

*House Agriculture Committee  
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*Testimony of  
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I am pleased to have the opportunity to submit testimony on behalf of the American Sugar Alliance, the national coalition of growers, processors, and refiners of sugarbeets and sugarcane.

The policy that Congress provided for the U.S. sugar industry in the 2002 Farm Bill has worked well.

- It has worked well for American taxpayers.
- It has worked well for American sugar consumers.
- And it has given American sugar farmers a chance to survive.

The industry and the policy have survived some major challenges over the past few years.

- A disconcerting 3-year decline in sugar consumption during 2001-2003 coincided with some unusually large crops and caused a huge buildup in producer-held stocks of sugar in 2004 and 2005.

But sugar consumption has rebounded strongly. After average annual declines of more than 150,000 tons during 2001-2003, consumption has been growing at a robust rate of about 200,000 tons per year since then (*Figure 1*).

- The threat of large imports of sugar from Mexico under the NAFTA, and from Central America under the CAFTA, and possible mandates for more sugar imports in other free trade agreements caused uncertainty in the market.

But during CAFTA consideration the Administration assured Congress that it would not allow unneeded imports from Mexico or under other FTAs to jeopardize the no-cost operation of sugar policy for the remainder of the 2002 Farm Bill, and officials said these assurances would be extended if the policy is extended. We are pleased to have these assurances. Nonetheless, challenges on the NAFTA front remain.

- An unprecedented string of natural disasters – drought in the West, excessive rains in the upper Midwest, and three hurricanes that ravaged Louisiana and Florida – sharply reduced domestic production.

But USDA responded to the coincidence of added demand and reduced supply in a manner that has defended both taxpayers and consumers. To their credit, USDA and the industry took immediate, effective steps to avoid a serious supply interruption.

- USDA allowed producers to release onto the market the half million tons of sugar producers had been required to store to balance the market.
- USDA more than doubled imports. We are now the world's second largest sugar importer.
- Cane refiners damaged by the hurricane worked frantically, with important help from USDA, to care for their workers and get their operations up and running again.

Recent USDA actions regarding import access for Mexico, and all quotaholders, appear to have oversupplied the market and raised new uncertainties.

But throughout this past year, American consumer sugar supplies remained reliable and high in quality and U.S. sugar policy continued to operate at no cost to taxpayers. The policy has shown its adaptability to challenging circumstances and that should continue.

### **Background: Industry Size, Efficiency, Restructuring**

The U.S. sugar producing industry accounts for 146,000 jobs in 19 states and generates \$10 billion in annual economic activity. Sugar is vital to the economies of many states and localities. In states such as Louisiana and Wyoming, sugar accounts for about 40% of the state's total crop receipts. Sugar accounts for 11-24% of all crop receipts in seven other states. There are small towns in every state that would most likely wither and die if they lost their sugarbeet or sugarcane processing plants.

The United States is the world's fifth largest sugar producer and consumer and second largest importer. U.S. production is about evenly divided between sugarbeets, grown in twelve mostly northern-tier states, and sugarcane, in four southern states.

Two decades of declining real prices for our product have forced U.S. producers to reduce costs. We have done so through investment in yield-improving technology, in the field and in the factory – beet and cane sugar yields per acre are up by more than a third since the early 1980's – and through a wrenching industry restructuring over the past several years.

Beet and cane growers throughout this nation are among the most efficient sugar producers in the world. We are particularly proud that we achieve this efficiency while complying with the world's highest labor and environmental standards and despite the strong dollar relative to the developing countries that dominate the world sugar market.

According to LMC International's global 2004 survey, beet growers in the Red River Valley of Minnesota and North Dakota are the most efficient beet growers in the world. U.S. beet sugar producers, as a whole, are third lowest cost of 41 producing countries or regions; U.S. cane sugar producers in the top third in efficiency among cane-producing countries, virtually all of them developing countries with low social standards and costs.

In the late 1990's, even nominal sugar prices were extremely low (*Figures 2, 3*), and this accelerated the industry restructuring. Just since 1996, more than a third of all U.S. beet and cane processing mills and cane sugar refineries have closed (*Figure 4*). Independent beet processors and cane sugar refining companies sought to exit the business. When no potential buyers emerged, beet and cane growers, alarmed they would have no place to deliver their sugarbeets and raw cane sugar, organized cooperatively to purchase beet processing plants and cane refineries. Growers are the last investors in the U.S. sugar industry – a warning sign of how fragile the industry has become.

Just between 1999 and 2005, the grower-owned share of U.S. total sugar refining capacity more than doubled, from 34% to 84%. Growers' share of cane sugar refining capacity shot up from 14% to 73%; beet growers' ownership of beet processing capacity became complete, climbing from 62% to 100%. While this enables the growers/processors to achieve greater efficiencies, the enormous amount of investment involved makes the growers more dependent than ever on maintaining a stable sugar market in the U.S.

### **Background on U.S. Sugar Policy**

In the 2002 Farm Bill, the United States Congress, by resounding majorities in both chambers – 71% of the votes cast in the Senate and 57% in the House – passed a successful sugar policy. Congressional support of U.S. sugar policy is growing. The House defeated an anti-sugar amendment in June 2005 with 66% of the votes cast. In May 2006, the House defeated an anti-sugar policy amendment by a vote of 281-135, or 68% of votes cast – the widest margin of any House sugar vote in decades.

U.S. sugar policy is unique among U.S. commodity programs. Under all commodity programs, the government offers farmers operating loans which they can satisfy by repaying the loan with interest or by forfeiting to the government the crop they put up as collateral. While other programs also provide income support to farmers when market prices fall below the loan rate, sugar policy does not, and is designed to run at no cost to the government by avoiding loan forfeitures.

Sugar policy is an inventory management program. The Secretary of Agriculture has two tools to manage the market: a WTO-legal tariff-rate quota (TRQ) to control imports, and a marketing allotment program to control domestic supplies.

The TRQ is a tool of limited use. The government cannot reduce imports below the minimum to which it has committed in trade agreements. At the time the 2002 Farm Bill was written this minimum was: 1.256 million short tons in the WTO and up to 276,000 tons of surplus production from Mexico in the NAFTA. Since then, the U.S. has conceded guaranteed access for 120,000 tons from six CAFTA countries, growing by 3,830 tons per year.

Essentially by subtracting required imports from anticipated consumption, and allowing for reasonable stock levels, USDA calculates the amount of sugar that could be marketed each year without the risk of depressing prices and inviting loan forfeitures. Farmers can plant as many acres of beets and cane as they want, and process as much sugar as they want, but they may not be able to sell it all onto the market. Sugar processors must store, at their own expense, whatever USDA judges to be in excess, until the market requires the sugar.

When Congress designed sugar policy in the 2002 Farm Bill, it specified that marketing allotments would be triggered off if imports rise above 1.532 million short tons, the total of U.S. import requirements at that time, and if those imports forced a reduction in allotments. Congress essentially was sending a message that this required import amount, about 15% of U.S. sugar consumption, was enough. Imports could grow if U.S. sugar consumption growth outstrips U.S. production growth, or if there is a crop shortfall. But U.S. producers should not have to cede larger minimum shares of their market to foreign producers.

**CAFTA and Sugar Policy.** CAFTA or other bilateral or regional free trade agreement (FTA) concessions, on top of the WTO and NAFTA concessions, could trigger off marketing allotments and endanger no-cost operation of sugar policy. The additional 120,000 short tons of access granted to CAFTA countries exceeded the limits on the import concessions that Congress envisioned.

The Administration did, however, prior to CAFTA's passage in July 2005, promise that the new FTAs would not jeopardize no-cost operation of U.S. sugar policy, at least in the short run.

In a June 29, 2005, letter to Chairman Goodlatte and Senate Agriculture Committee Chairman Chambliss, Secretary Johanns provided assurance that "the DR-CAFTA will not interfere with USDA's ability to operate the sugar program in a way that provides the full benefit to domestic growers through the remainder of the 2002 Farm Bill. If the Farm Bill import trigger is exceeded and the domestic market is adequately supplied with sugar, then the excess imported sugar up to an amount equivalent to DR-CAFTA imports will be purchased by CCC and made available for conversion to ethanol." Secretary Johanns also promised a USDA study on "the feasibility of converting sugar into ethanol," which was issued in July 2006.

Secretary Johanns noted that his assurance would apply to "imports from NAFTA, CAFTA, and other trade agreements" in addition to the import trigger amount of 1.532 million short tons. This assurance is valuable because of the added danger to the program's operation posed by above-quota imports from Mexico and by additional concessions since negotiated in FTAs with Colombia (55,115 short tons) and Peru (12,125 short tons) (*Figure 5*).

The U.S. sugar market was able to absorb additional CAFTA sugar and Mexican above-quota imports this past year because of the sharp drop in domestic production in 2005/06, and USDA has not needed to divert any imported sugar to nonfood uses. But a return to more normal domestic production, as we appear to be witnessing this year, could result in excessive NAFTA and CAFTA imports creating serious oversupply problems.

If the sugar provisions of the 2002 Farm Bill are extended in next Farm Bill, as we recommend, we are pleased that we have the commitments the Secretary made during CAFTA consideration that the Administration would continue to take steps to protect the no-cost operation of U.S. sugar policy.

### **Trade Policy Concerns**

American sugar producers are rueful about the reality that, while they are efficient and would like to become more so by increasing throughput and minimizing unit costs, U.S. trade policy constrains them from doing so. With a large segment of the U.S. market reserved for imports,

American producers are residual suppliers of their own market. To make matters worse, there is enormous political pressure to increase imports and no prospect of reducing them.

**FTAs.** In addition to the CAFTA, which cedes 120,000 short tons of our market in the first year, growing to 169,000 tons per year within the next 15 years, the Administration is at various stages of negotiating bilateral or regional FTAs with 21 other sugar-exporting countries. These countries produced an annual average of 50 million tons of sugar during 2003/04-2005/06. They exported 25 million tons per year – nearly triple U.S. sugar consumption. All these countries already enjoy guaranteed shares of the U.S. sugar-import quota, essentially duty-free.

The Congress, and the American sugar industry, do not believe the U.S. sugar market should be carved up for subsidized foreign sugar producers, particularly without addressing the subsidies in those countries. The U.S. sugar industry urges that the Administration either exclude sugar from future FTA negotiations, or ensure that the import concessions that are granted in these agreements do not depress the U.S. sugar market. These agreements do nothing to level the playing field in the highly distorted world market for sugar.

**WTO.** Sugar is the most distorted commodity market in the world. The government in every country that produces sugar intervenes in its sugar market in some way. The biggest producers, and subsidizers, dump their surplus on the world market for whatever price it will bring. As a result of this pervasive dumping, so-called world market prices for sugar have averaged barely half the world average cost of production over the past two decades (*Figure 6*).

A table attached to this testimony summarizes an extensive study on direct and indirect subsidies among the major sugar producing and countries. It illustrates how pervasive and diverse these many forms of sugar subsidy are (*Figure 7*).

No producer could survive at prices so low. But government intervention ensures that domestic wholesale prices, at which most sugar is sold, are well above world dump market levels. Globally, domestic clearing prices for sugar average 22 cents per pound – double the historic world dump market price and virtually the same as the U.S. refined beet sugar support price of 22.90 cents per pound (*Figure 8*).

The sugar subsidy problem is a global problem. It must be addressed globally in the WTO – comprehensive, multilateral, sector-specific negotiations – all countries, all programs. The industry has supported the WTO approach since the onset of the Uruguay Round in 1986.

Piecemeal market access concessions in bilateral and regional free trade agreements will *not* help solve the global sugar subsidy problem. Such concessions could, however, put the U.S. sugar industry out of business while foreign subsidies continue unchecked.

*Doha Round.* Doha Development Round negotiations are suspended. Talks could be resumed, but changes in the Doha Round approach must be made if fundamental reform of the world sugar market is to be achieved. There are at least three areas where the Doha negotiations seem likely to fall well short of serious foreign sugar policy reform:

- **Indirect subsidies.** Many of the most highly distorting foreign sugar policies are indirect and non-transparent and, thus, not easily reached by the formulaic approach being pursued in the negotiations. It seems highly unlikely that, if agreement on the basic

modalities is reached, there will be sufficient energy, time, or leverage to pursue sectoral approaches.

- **Special treatment for developing countries.** Developing countries account for 75% of world sugar production and exports. But, given the extensive commitments to special and differential treatment and the opaque nature of most developing-country policies on sugar, such policies will be little affected by Doha.
- **“Special product” exemptions.** Furthermore, most sugar-producing developing countries will likely claim “special product” status for sugar to avoid opening their own markets to imports.

In the absence of comprehensive reform of the policies distorting the world sugar market, there is little justification for major changes in the U.S. sugar program or for weakening U.S. protection from the world “dump market” for sugar.

**NAFTA.** The 15-year NAFTA phase-in will end in 2008 with the elimination of all barriers to trade in sugar and corn sweeteners. Up until then, U.S. imports of Mexican sugar are limited to up to 250,000 metric tons of surplus Mexican sugar – surplus production defined as Mexican sugar production minus Mexican sugar and corn syrup consumption.

Under NAFTA, U.S. producers of U.S. high-fructose corn syrup (HFCS) should have enjoyed duty free access to Mexico since 2003. Mexico, however, levies a 20% tax on soft drinks made with anything but cane sugar and the tax has acted as a barrier to U.S. HFCS shipments to Mexico. The WTO has ruled the tax illegal. Absent the tax, unlimited imports and use of corn sweetener in Mexico could displace as much as 2 million tons of Mexican sugar, wreck the Mexican sugar industry, and displace hundreds of thousands of Mexican sugar farmers. A flood of Mexican sugar into the United States would destroy the U.S. market.

The Mexican sugar industry, nearly half of which is still owned and operated by the Mexican government, is also concerned about competition with efficient American sugar producers. The U.S. enjoys duty-free access to Mexico for only 7,258 metric tons of sugar per year now, but we will be permitted to send unlimited quantities beginning in 2008.

**U.S.-Mexican Agreement.** The U.S. and Mexican governments announced a deal last July aimed at smoothing the transition to free trade in 2008. Mexico agreed to lift its soft-drink tax in 2007, and to import large quantities of U.S. HFCS -- 250,000 metric tons in 2006/07 (Oct-Sep) and at least 175,000 in the final quarter of 2007. The U.S. agreed to accept like quantities of Mexican sugar. The agreement also called for the creation of a joint industry/government task force to develop a program for stable sweetener market integration beyond 2008.

The U.S. sugar industry endorses full compliance with international trade rules and commends Mexico’s promise to lift its soft drink tax. We have, however, expressed some misgivings to the Administration regarding the July agreement.

- The U.S. has ignored explicit NAFTA rules limiting Mexican duty-free sugar access to the U.S. to Mexico’s surplus sugar production. Published USDA statistics show Mexico to be a significant *deficit* producer in 2005/06 and 2006/07; moreover, the Mexican government recently announced it is increasing Mexican sugar imports by 110%.

Nonetheless:

- The U.S. had already granted Mexico 340,000 metric tons of guaranteed duty-free access in 2005/06.
  - The U.S. has granted 250,000 tons of access in 2006/07.
  - The U.S. has granted 175,000-250,000 tons of access in the first quarter of 2007/08, though no statistics are available yet for that year.
- The guaranteed amounts granted to Mexico appear likely to exceed U.S. sugar market needs. U.S. sugar prices are off sharply since the agreement was announced – strong evidence the market regards the amounts granted as overly generous.

Other victims of providing excess access to Mexico are the other 40 quotaholding countries, virtually all developing, that have traditionally been guaranteed access to the U.S. sugar market. Some of these have expressed their concern to the Administration that the amounts granted to Mexico are their expense and are in violation of NAFTA and WTO rules.

Nonetheless, the U.S. sugar industry is encouraged by the agreement's planned formation of a task force to consider U.S.-Mexican sugar trade beyond 2007. The governments of both countries apparently recognize the danger that unmanaged trade flows could pose to their sweetener industries – market oversupply, price collapse, and vulnerability to subsidized world dump market sugar. The U.S. marketing allotment system may prove to be the model for the future for both countries. We look forward to pursuing these discussions.

*Sugar policy survival after 2008.* Some observers have predicted that U.S. sugar policy will collapse under a deluge of Mexican sugar after 2008 when restrictions are lifted on U.S. corn sweetener exports to Mexico and on Mexican sugar exports to the U.S. These circumstances do pose a major challenge to the continued no-cost operation of sugar policy. But reports of our pending demise are exaggerated. There are a number of reasons U.S. sugar policy may be able to continue in basically its current form beyond 2008:

1. **Sugar trade with Mexico becomes a two-way street.** The U.S. can send Mexico unlimited amounts of sugar, duty-free, beginning January 1, 2008. Mexico is an appealing market for U.S. producers:
  - Sugar prices in Mexico are higher than here and have been for years.
  - Mexico's population and income growth rates are high.
  - U.S. producers are more efficient and market oriented, and unsubsidized by our government.
  - The U.S. produces a higher quality refined sugar.
2. **Mexico may not have much sugar to export.** The domestic market is in deficit and the industry has not been able to fulfill generous concessions the U.S. has provided for duty-free access to the U.S. sugar market. The Mexican government is aggressively importing sugar from the world dump market to satisfy domestic needs and while it sends Mexican production to the U.S. The substitution of foreign sugar for Mexican is technically not illegal, but it represents another example of Mexico abusing the intent of the NAFTA.
3. **The quality of Mexican refined sugar is low.** American sugar users who imported large quantities of Mexican refined sugar last year were keenly disappointed in its quality.

Impurities, such as metal shavings, fiber from burlap sacks, and other trash, meant the sugar had to be re-refined in the U.S. Users accustomed to bulk refined sugar deliveries from U.S. producers also had problems with Mexican sugar in large bags. These factors could significantly limit U.S. demand for Mexican refined sugar.

4. **Mexico may not allow unlimited quantities of U.S. HFCS into its market.** Mexico has promised to lift its soda tax, through Congressional action, in 2007. But President Fox has repeatedly asked the Mexican Congress to lift the tax in years past, and it has never done so. If the soda tax is not repealed – or it is replaced by some other creative trade barrier – and the Mexican beverage industry continues to use sugar, Mexico could have little, if any, surplus sugar available to send to the U.S.
5. **The U.S. may not have large quantities of surplus HFCS to sell to Mexico.** USDA's chief economist recently told a Congressional Committee he expects U.S. corn prices to hit record levels because of soaring demand for ethanol. Competition with the livestock and ethanol sectors for increasingly costly corn supplies could limit the growth of U.S. HFCS operations.
6. **The Mexican industry is egregiously subsidized.** In 2001, years after the NAFTA had been negotiated, the Mexican government nationalized nearly half the Mexican sugar industry, primarily to save it from bankruptcy. The U.S. industry and government will not look approvingly at a flood of sugar from an industry where nearly half the sugar mills continue to be owned and operated by the Mexican government.
7. **The U.S. can stop Mexican dumping.** A flood of Mexican sugar could ruin the U.S. sugar industry and undermine the long-term security of our homegrown food supply. The U.S. would respond to a flood of subsidized Mexican sugar with anti-dumping and countervailing-duty petitions to prevent injury. With the Mexican government's extreme involvement in its sugar industry and Mexico's higher price structure, the U.S. would have overwhelming justification for this type of trade remedy.
8. **Sugar and corn industries in both countries could be harmed.** Wholesale refined sugar prices are currently around 40 cents per pound in Mexico and 30 cents per pound in the U.S.; U.S. spot prices for HFCS-55 (the sweetener equivalent of sugar) are 17-18 cents. World dump market sugar prices, meanwhile, have been running about 11 cents per pound, raw value. Floods of excess sugar that push U.S. and Mexican sugar prices down to world dump market levels would not only wreck the sugar industries of both countries, but would also seriously undermine the profitability of the U.S. corn sweetener sector.
9. **Both governments are committed to orderly markets beyond 2008.** In the agreement forged last July, the Mexican government requested, and the U.S. government concurred, that a joint government-industry task force should be created to monitor the market. This government-industry task force could provide a framework for preventing a North American sweetener trade disaster in the future.

These factors do not guarantee there will be smooth sailing for U.S. Mexican sweetener trade after 2008. But they should indicate it is unfair to assume that U.S. sugar policy will necessarily implode at that time.

## Sucrose Ethanol Solution to Trade Policy Pressures?

With oil, gasoline, and ethanol prices at record highs, and with sugar and other agricultural commodities generally in surplus, a sucrose ethanol program deserves serious examination. USDA released a study on the efficacy of a sucrose ethanol program in the United States last July.

USDA did not lay out a plan for a U.S. sucrose ethanol program, but it did examine some relative cost issues. Based on USDA findings and our own views, we would make the following observations:

- Ethanol can be produced competitively from U.S. sugar, at U.S. sugar prices, but only when ethanol prices are high. U.S. ethanol prices have declined over the past two months from \$4.00 per gallon to about \$2.50 per gallon. USDA found that ethanol can currently be produced from U.S. cane and beets for \$2.35-2.40 per gallon; from U.S. corn for \$1.03-1.05 per gallon; and from Brazilian cane for \$0.81 per gallon. Ethanol prices cannot be expected to remain high indefinitely, and potential U.S. producers are unlikely to invest in building production capacity on the assumption of long-term high prices. The exception is Hawaii, where added state incentives are encouraging investment in the adaptation of cane mills for ethanol production.
- The lowest cost ethanol production in the world is in Brazil, from sugarcane. Brazil benefits from 30 years of government subsidies, investment, and consumption mandates that have eliminated Brazilian dependence on foreign oil. Brazil is the world's largest cane producer and more than half its cane goes to ethanol. This makes sugar a byproduct of the Brazilian cane industry and allows Brazil to price sugar extremely cheaply, for food or for ethanol. Brazil's cheap-sugar policy and years of government and private sector investment in capacity and technology have made Brazil the low-cost ethanol producer.
- U.S. ethanol production from corn is more costly than Brazilian ethanol from cane, but less costly than U.S. ethanol from sugar. The U.S. maintains relatively low corn prices to be competitive in world export markets. But, like all other sugar-producing countries, the U.S. maintains sugar prices higher than Brazil's. This puts U.S. sugar at a disadvantage to U.S. corn for ethanol production. U.S. corn also benefits from about 20 years of federal ethanol tax credits, plus state, and now federal, mandates for ethanol consumption, which have encouraged investment in ethanol mill construction and technology.

U.S. ethanol demand is growing so rapidly that feedstocks in addition to corn need to be considered. If the Administration or Congress is determined to reduce U.S. dependence on foreign oil and shift to domestic renewable resources, sugar should certainly be among the feedstocks considered. Future breakthroughs in the development of ethanol from cellulosic materials could make ethanol from sugar crops much more competitive.

The Administration has made clear that in order to complete trade agreements with sugar-exporting countries it will concede access to the U.S. market for sugar we do not need. An ethanol program for that surplus sugar could prove to be a viable complement to U.S. sugar policy relative to the Administration goals regarding trade policy and reducing U.S. dependence on foreign oil.

We would emphasize that any sucrose ethanol program the Administration might propose would be complementary to U.S. sugar policy. The U.S. sugar industry remains overwhelmingly committed to producing sugar for food and to maintaining the current structure of U.S. sugar policy.

### **U.S. Sugar Policy: Success for Taxpayers**

American sugar farmers are proud of the fact that sugar is the only major U.S. commodity program run at no cost to taxpayers. We derive all our returns from the marketplace. We receive no income supports from the government to cushion the blow when market prices drop. We have not had an increase in our support price in 21 years, though inflation since 1985 has been 81%.

### **U.S. Sugar Policy: Success for Consumers**

American consumers get a great deal on sugar. Consumer prices are low and affordable by world standards, and extremely stable. Foreign developed-country consumers, on average, pay 30% more for their sugar than American consumers do. And, remarkably, U.S. retail sugar prices are essentially unchanged since the early 1990's. In terms of minutes of work to purchase a pound, sugar in the U.S. is about the most affordable in the world (*Figures 9, 10*).

The retail sugar prices in Australia and Canada are worth noting. These countries tout their free-trade nature and their exposure to low-priced world dump market raw sugar, and imply consumer benefits from this exposure. Yet their consumer prices for refined sugar are virtually identical to the United States' 43 cents per pound: Australia at 43 cents and Canada at 42 cents. As would be the case in this country, the benefit of access to low-priced raw sugar clearly accrues to food manufacturers and retailers, not to consumers.

Even after the shock to the U.S. sugar supply chain from the weather disasters in 2005, U.S. retail prices still averaged 43 cents per pound – the same level as in 1990 and even in 1980.

American consumers' savings on sugar could be even greater, but history has shown that consumers do *not* benefit when producer prices for sugar fall: Grocers and food manufacturers routinely absorb their savings as higher profits rather than passing the lower sugar prices along to consumers. Food manufacturers have enjoyed retail price increases for sweetened products at least in line with inflation, while paying producers lower prices for the sugar the manufacturers buy (*Figure 11*).

Even if food manufacturers passed *all* their savings from lower sugar prices along to consumers, consumers would hardly notice. For example, there is about 1 cent worth of sugar in a 72-cent candy bar. If sugar prices were to fall by 10%, and the candy manufacturers and retailers passed along *all* the savings, the price of that 72-cent candy would fall to 71.9 cents. *If sugar producers gave the sugar to the candy manufacturers for free*, and the passthrough were 100%, the price of the 72-cent candy bar would plummet to 71 cents. The attached charts depict sugar's tiny share of retail product prices and similar potential price changes for a host of other sweetened products (*Figures 12, 13*).

## Higher Wholesale Prices in 2005/06

Food manufacturers complain that wholesale refined sugar prices have risen and that at times during the post-hurricane period supplies were tight. It is important to put these developments in perspective.

- The wholesale price increase has been only the third significant rise in the past 21 years – on a par with modest rises in 1989-90 and 1996 related to weather-related crop disruptions. Corrected for inflation, prices food manufacturers paid for sugar in 2005 were 30% lower than in 1985 (*Figure 3*). A number of sweetened food manufacturing corporations announced record profits in 2005 – some noted sugar was an insignificant cost for them, others that they had booked their 2005/06 sugar purchases at low pre-hurricane price levels.
- Food manufacturers have, in effect, been victims of their own success. In bringing policy pressure to keep producer prices for sugar low the past two decades, they have forced many producers out of business (38% of all sugar production facilities have closed just since 1996) and reduced capacity. Manufacturers have demanded just-in-time delivery, shifting storage burdens from the manufacturers to the producers. The low prices and reduction in storage costs have reduced food manufacturers' overall costs, but made them more vulnerable to transportation and producer-facility disruptions.
- The food manufacturers have demanded extremely high-quality sugar and this has made them vulnerable to the type of quality problems they have experienced with imported refined sugar.
- Their first market price rise in 10 years is enabling producers to cope with soaring costs for fuel, fertilizer, and weather damage and, perhaps, buy down some of their debt.

The lesson to the food manufacturers, and to Congress, is clear: If food manufacturers are to expect reliable high-quality supplies of refined sugar, they cannot afford to force more U.S. beet processors or cane refiners out of business.

## Policy Alternatives?

Despite sugar policy's continued success, even after being tested by last year's natural disasters, some would like to change the policy. Food manufacturers and retailers have been the biggest beneficiaries of the change in U.S. policy since 1996 for most commodities. Commodity prices have been allowed to fall, but farmers are kept afloat by government payments.

The food manufacturers get the cheapest possible raw commodities from reliable American farmers and, by not passing their savings along to consumers, increase their profit margins. The taxpayer cost of subsidizing food manufacturers this way has totaled over \$200 billion since 1996.

The U.S. sugar industry in no way is critical of the cash payment programs now operated for other commodities, and we are pleased that approach may be working well for those producers. But we reject the suggestion this is a model that sugar policy should follow. The sugar industry is different and a payment approach does not fit.

The U.S. sugar industry is more vertically integrated and characterized by larger farm operations in some areas of the country. For example, payment programs designed for farmers would have to be adapted for sugar processors, which are the entities that put sugar under loan. Payment limitations would also be a huge hurdle, since cane operations tend to be quite large, and many diversified beet farmers may already be at their payment limits for the other program crops they grow.

With the agricultural budget under enormous pressure for reductions, other commodity programs would have to be cut to make the money available to convert sugar policy from no cost to high cost.

As history has shown with sugar and other commodities, consumers do not benefit when raw ingredient prices fall. A conversion to the income-support approach for sugar would be another boon for the food manufacturers, but these already profitable corporations would be the sole beneficiary.

A recent independent analysis puts the cost of converting sugar to a standard program at \$1.3 billion per year (*"The Future of U.S. Sugar Policy,"* McKeany-Flavell Company, Inc., Oakland, CA, June 14, 2006). The study assumes that U.S. sugar prices fall to world dump market levels, which have averaged about 10 cents per pound for the past 20 years, but that U.S. sugar producers are kept afloat through income transfers from the government.

The Sweetener Users have suggested the study's world price assumption is too low, and the estimated cost of the program too high, because world prices rose to the upper teens earlier this year. But prices have since fallen back to 11 cents, reinforcing the volatile, dump nature of that market and the reasonability of the study's world price assumption. Should prices continue to fall, to below 10 cents, the cost of the standard program for sugar would be still higher than the estimated \$1.3 billion.

We would like to submit for the record an Issue Brief explaining in more detail why the payment approach does not fit for sugar – it is entitled: *"Sugar Subsidy Checks are Unworkable."*

**Food manufacturers' sugar policy proposals.** The Sweetener Users Association, which testified before this Committee a week ago, has acknowledged the importance of maintaining a viable and efficient U.S. sugar-producing industry. They have testified they do not want to see our industry shrink any further. We are pleased with their commitment to the continued viability of the producer industry. We have met with them about the future of sugar policy and may continue to meet.

Their policy proposals are geared to achieve the noble goal of preventing further decline in our industry, but at they would do so at considerable taxpayer cost.

The Users have suggested three policy alternatives:

- Standard Commodity Program (direct payments, countercyclical payments and loan deficiency payments);
- Revenue Assurance;
- Direct Payments.

In each case, the U.S. price would be permitted to drop to the world price, but government payments to sugar producers would compensate for their drop in income. The Users assume that, unlike all other standard commodity programs, payment limitations would not apply to sugar producers. The Users have not estimated what each approach would cost, but annual taxpayer costs around the \$1.3 billion estimated by McKeany-Flavell would be likely.

In our view, the political and economic costs of converting a no-cost sugar policy to a no-payment-limitation, high-taxpayer-cost policy would be insurmountable. We welcome the Committee's views on this issue.

Moreover, the cotton case has shown that the U.S. standard program is vulnerable to WTO challenge. The revenue assurance and direct payment approaches may be as well.

At a time when Congress is facing two key hurdles to maintaining a strong safety net for farmers and ranchers – budget pressures and WTO compliance – these proposals could add costs, as well as WTO exposure, where little to none exists today.

*Developing-country damage.* Perhaps the biggest loser from the Sweetener Users' approach on sugar policy, after the American taxpayer, would be the 41 foreign quotaholder countries – 39 of which are developing countries. The U.S. government would supposedly compensate American sugar producers for the drop in their price to the world dump market level, but these sugar-exporting countries would receive nothing.

The real value of these countries' guaranteed access to the U.S. market – a premium of about 10 cents per pound – would disappear. Aside from Brazil, with its ethanol subsidies, none of these countries can produce sugar at traditional world price levels and the sugar industries in the countries most dependent on access to the U.S. market – such as the Dominican Republic, the Philippines, Jamaica, Mauritius, and others – could collapse.

## **Conclusion**

U.S. sugar policy is working for American taxpayers and consumers. It is giving American sugar growers a chance to survive in a highly subsidized and distorted world market.

The greatest threats to continued no-cost operation of this successful policy are NAFTA integration and the horde of FTAs with sugar-exporting countries that could carve up our market to subsidized foreign producers, without addressing any of the foreign subsidies that so badly distort the world market. NAFTA challenges have the potential to be addressed through reasoned U.S.-Mexican dialogue. And foreign distortions can be addressed, but that can only occur in the multilateral context of the WTO.

We urge that the highly successful no-cost U.S. sugar policy be allowed to continue.

Figure 1

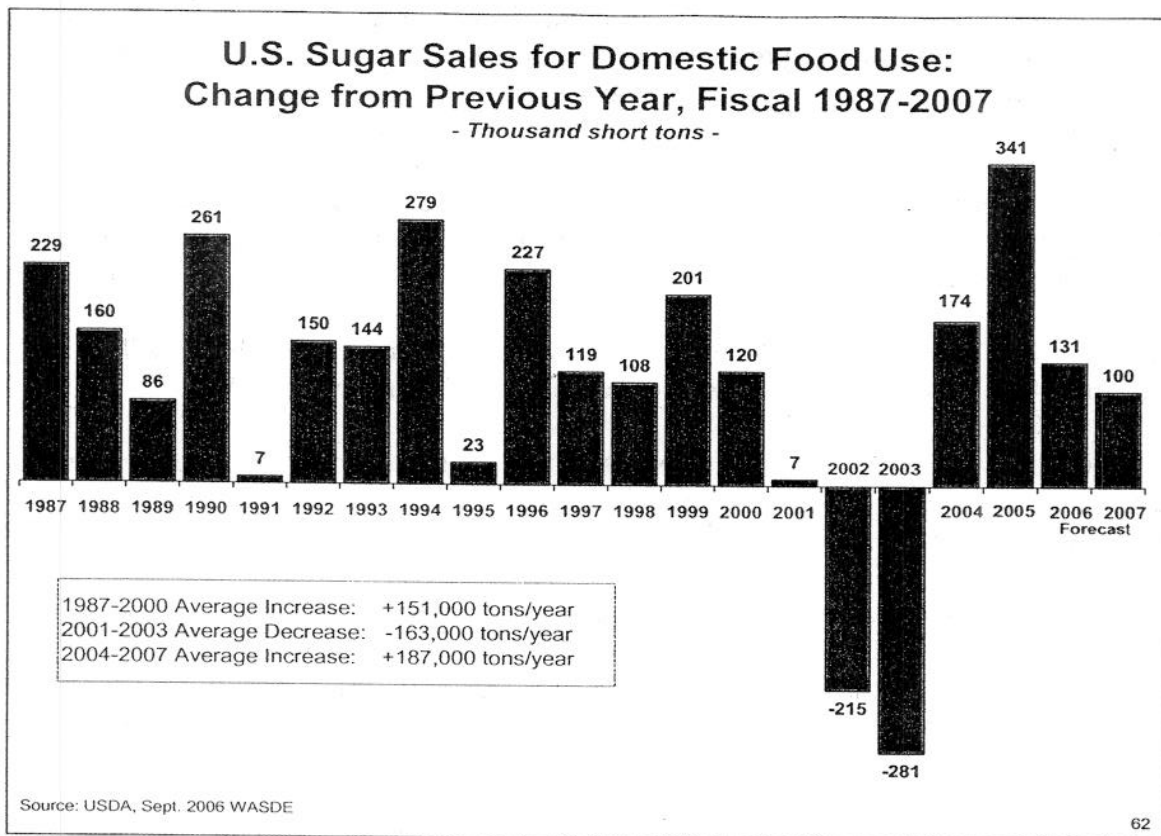


Figure 2

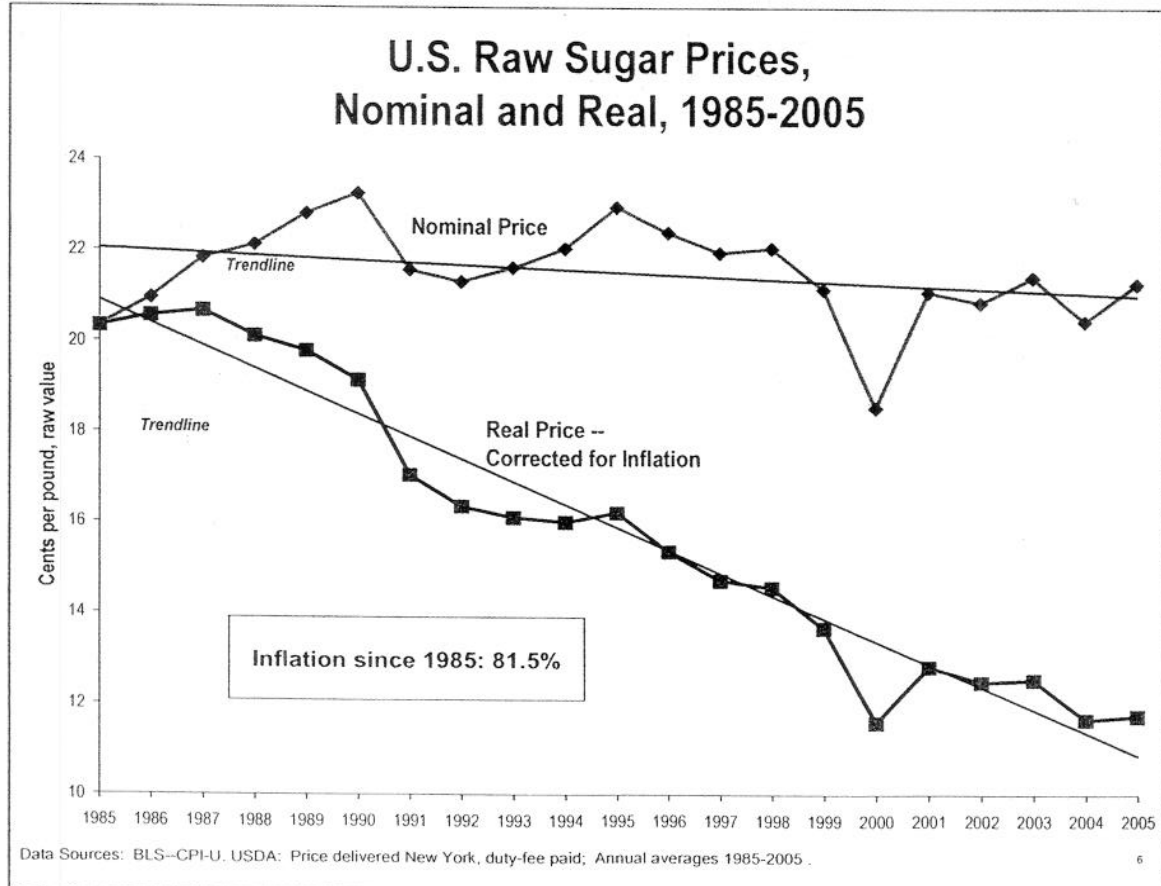


Figure 3

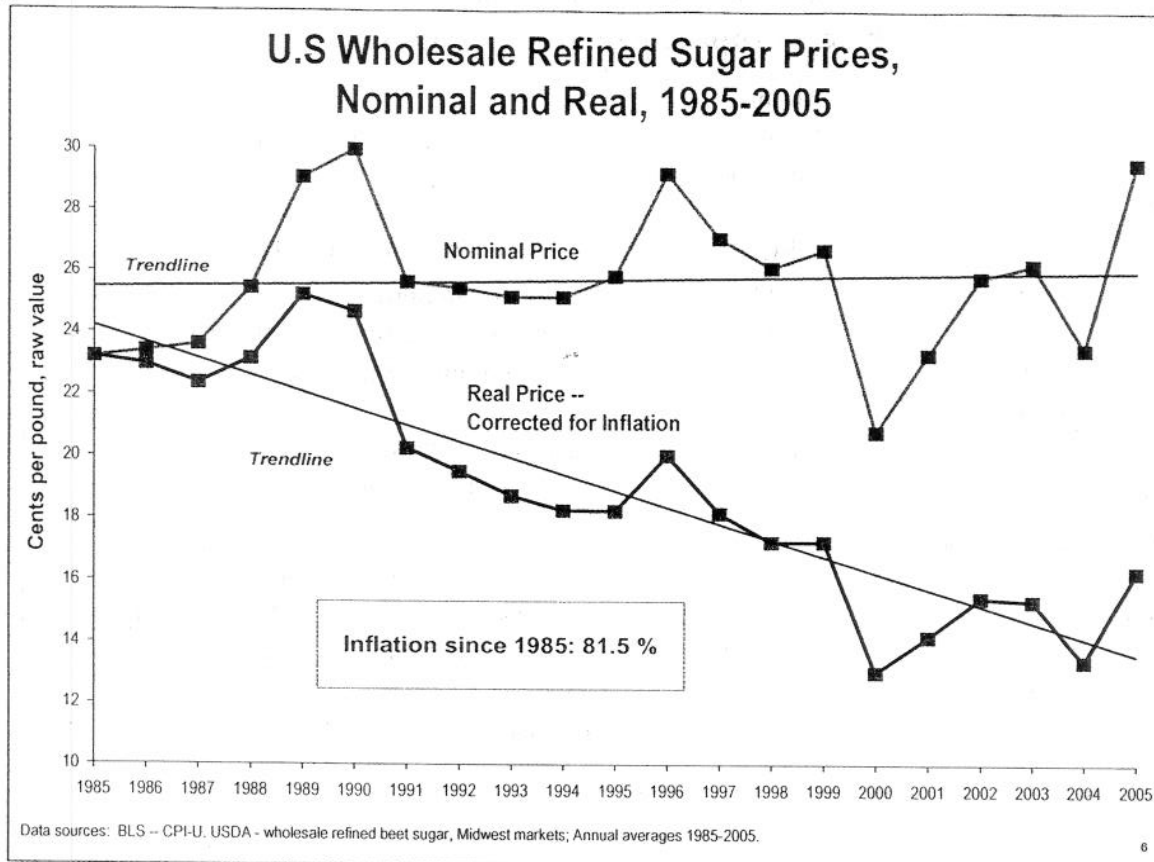


Figure 4

33 Sugar Mill and Refinery Closures Since 1996		
BEET CLOSURES	CANE CLOSURES	
Spreckels Sugar, Manteca California, 1996	Ka'u Agribusiness Hawaii, 1996	Evan Hall Sugar Cooperative Louisiana, 2001
Holly Sugar, Hamilton City California, 1996	Waialua Sugar Hawaii, 1996	Caldwell Sugar Cooperative Louisiana, 2001
Western Sugar, Mitchell Nebraska, 1996	McBryde Sugar Hawaii, 1996	Glenwood Sugar Cooperative Louisiana, 2003
Great Lakes Sugar, Fremont Ohio, 1996	Breaux Bridge Sugar Louisiana, 1998	New Iberia Sugar Cooperative Louisiana, 2005
Holly Sugar, Hereford Texas, 1998	Pioneer Mill Company Hawaii, 1999	Jeanerette Sugar Company Louisiana, 2005
Holly Sugar, Tracy California, 2000	Talisman Sugar Company Florida, 1999	U.S. Sugar, Bryant Florida, 2005*
Holly Sugar, Woodland California, 2000	Amfac Sugar, Kekaha Hawaii, 2000	Cinclare Central Facility Louisiana, 2005*
Western Sugar, Bayard Nebraska, 2002	Amfac Sugar, Lihue Hawaii, 2000	Atlantic Sugar, Belle Glade Florida, 2005**
Pacific Northwest, Moses Lake Washington, 2003	Hawaiian Commercial & Sugar, Paia Hawaii, 2000	
Western Sugar, Greeley Colorado, 2003	CANE REFINERY CLOSURES	
Amalgamated Sugar, Nyssa Oregon, 2005**	Aiea, C & H Hawaii, 1996	Sugarland, Imperial Texas, 2003
Michigan Sugar, Carrollton Michigan, 2005**	Everglades, Imperial Florida, 1999	Brooklyn, Domino New York, 2004

\*Phasing out operations, 2005-07. \*\*Suspended operations for 2005/06.  
Note: In 2006, 23 beet factories, 19 raw cane mills, and 8 cane refineries remain in continuous operation, a 39% drop since 1996.  
American Sugar Alliance, March 2006.

**Figure 5**

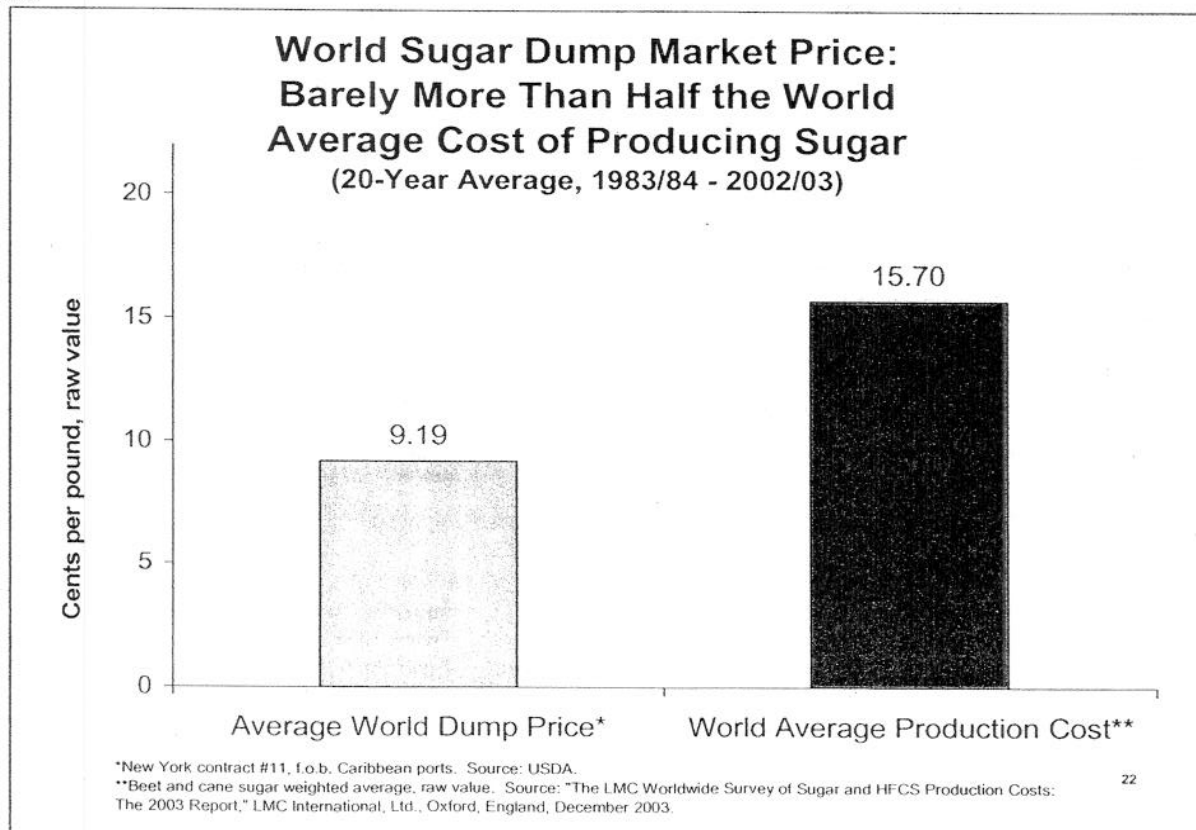
<b>U.S. Import Concessions: In Place, Proposed, or Being Negotiated</b>		
	Import Amount <i>-Metric tons-</i>	Comment
<u>In Place</u>		
WTO (41 Countries)	1,154,192	Could rise in Doha Round
NAFTA - Mexico <sup>1</sup>	250,000	Unlimited in 2008
CAFTA	109,000	Grows by 3,475 mt/yr years 2-15; by 2,640 mt/yr thereafter
<u>Not yet approved</u>		
Peru	11,000	Grows by 180 mt/yr forever
Colombia	50,000	Grows 750 mt/yr forever
<u>Being, or to be, negotiated</u>		
Panama	?	Exports 40,000 mt/yr, 3/4 to U.S. duty free
Ecuador	?	Exports 48,000 mt/yr, 1/4 to U.S. duty free
Thailand	?	World's 3rd largest exporter
South Africa/Swaziland	?	Export 1.4 mmt/yr
FTAA <sup>2</sup>	?	Exports 22 mmt/yr

<sup>1</sup> Up to 250,000 tons of surplus production, through 2007.

<sup>2</sup> Free Trade Area of the Americas -- 24 sugar exporting countries.

73

**Figure 6**



22

Figure 7

Summary of Support for Sugar Industry in Selected Countries, 2002<sup>1</sup>

	Australia	Brazil <sup>7</sup>	China <sup>8,9</sup>	Colombia	Cuba	EU <sup>10,11</sup>	Guatemala	India <sup>12</sup>	Indonesia	Japan	Mexico	Russia	S. Africa	Thailand	Turkey
<b>TRANSPARENT SUPPORT</b>															
Domestic Market Controls															
Production Quotas						✓		✓	✓	✓				✓	✓
Guaranteed Support Prices			✓			✓		✓	✓					✓	✓
Supply Controls								✓							
Market Sharing/Sales Quotas				✓			✓				✓		✓		
<b>Import Controls</b>															
Import Quota			✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Import Tariff		✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Import Licences			✓						✓						
Quality Restrictions							✓			✓					
<b>Export Support</b>															
Export Subsidies				✓		✓		✓					✓		✓
Single Desk Selling	✓		✓	✓	✓								✓		
<b>NON-TRANSPARENT SUPPORT</b>															
<b>Direct Financial Aid</b>															
State Ownership					✓					✓	✓			✓	✓
Income Support	✓	✓				✓								✓	
Debt Financing <sup>1</sup>	✓	✓								✓	✓	✓	✓	✓	✓
Input Subsidies <sup>2</sup>								✓	✓		✓	✓	✓	✓	✓
<b>Indirect Long Term Support</b>															
R&D Subsidies	✓	✓		✓		✓		✓					✓		✓
Efficiency Programs															
Ethanol Programs/Subsidies															
Consumer Demand Support															
Average Production, 2000-02 (mmt, raw value)	4.9	19.3	7.9	2.3	3.8	18.0	1.8	19.9	1.6	0.8	5.1	1.7	2.7	5.8	2.3
Rank Among World Producers	8	2	4	13	9	3	16	1	20	24	7	18	11	6	12
Average Exports, 2000-02 (mmt, raw value) <sup>9</sup>	4.5	9.5	0.4	0.9	3.0	5.7	1.2	0.1	-	-	0.7	0.1	1.1	3.0	0.4
Rank Among World Exporters	3	1	15	8	4	2	6	42	-	-	9	33	7	5	13
Domestic Wholesale Sugar Price (cents/lb) <sup>10</sup>	13.5	8.1	16.9	21.1	0.1	30.4	18.0	12.7	19.8	65.4	25.6	16.5	17.3	11.8	27.9
Import Tariff Level (refined, a.v. or equivalent) <sup>11</sup>	0%	18%	75%	20%	10%	164%	20%	68%	20%	71%	172%	50%	46%	96%	138%

Notes: 1. Policy information for countries was collected in June 2003, with the exception of Indonesia, which is based on the 2004/05 season.

2. Includes low interest loans, interest rate subsidies, debt relief and debt rescheduling.

3. Includes crop pre-financing, irrigation provision, land maintenance and inventory financing.

4. Japan is an importer of sugar only. It is the world's fourth largest importer of sugar, importing 1.6 million metric tons per annum on average between 2000 and 2002.

5. The Cuba wholesale price represents the heavily subsidised ration entitlement. All prices are for refined sugar.

6. Import tariffs reported in this line applied as of July 2005.

7. Brazil provides direct subsidies (income support) to producers in the North/North East region only.

8. Chinese cane and beet prices are controlled at the provincial level.

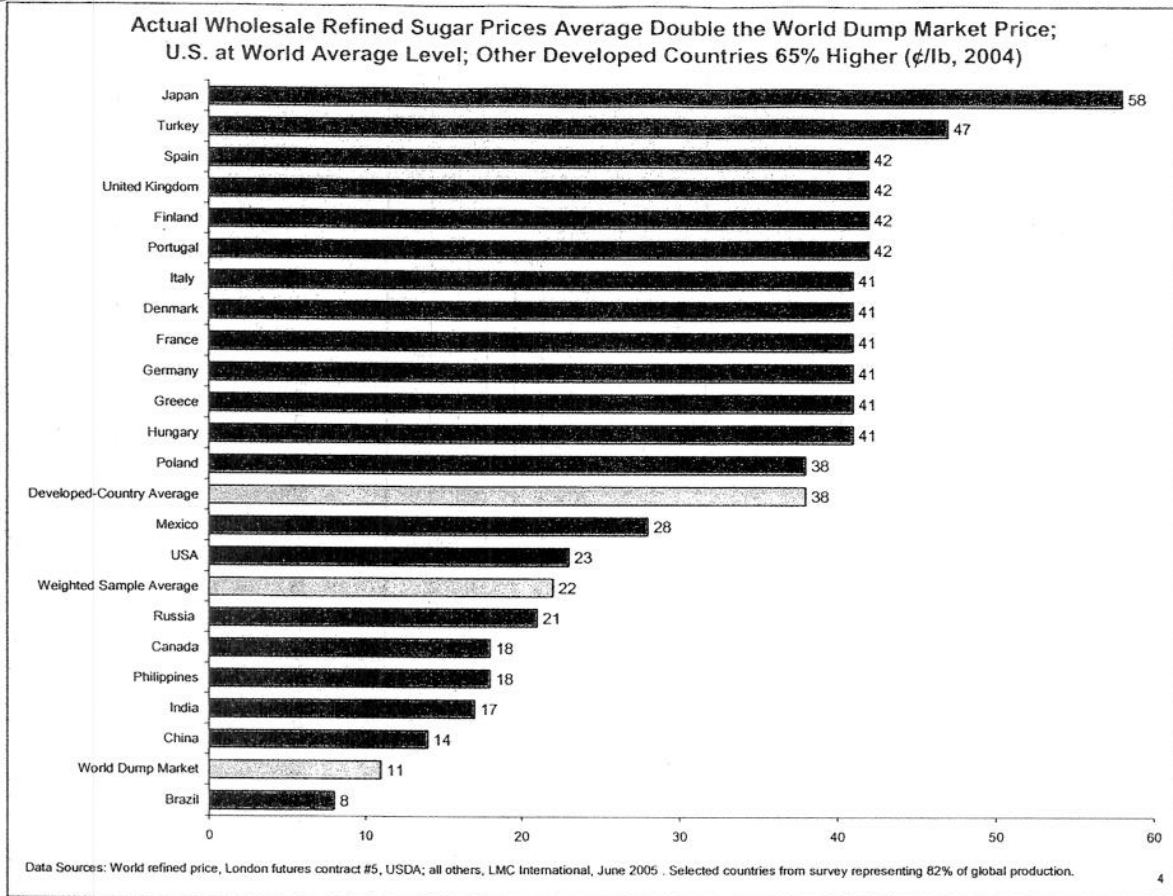
9. State trading companies account for 70% of domestic sales in China.

10. The EU provides an income support subsidy to refiners of cane sugar.

11. The EU Commission provides directives on ethanol use, though these are not binding.

12. India provides a transport subsidy for exporters.

**Figure 8**



**Figure 9**

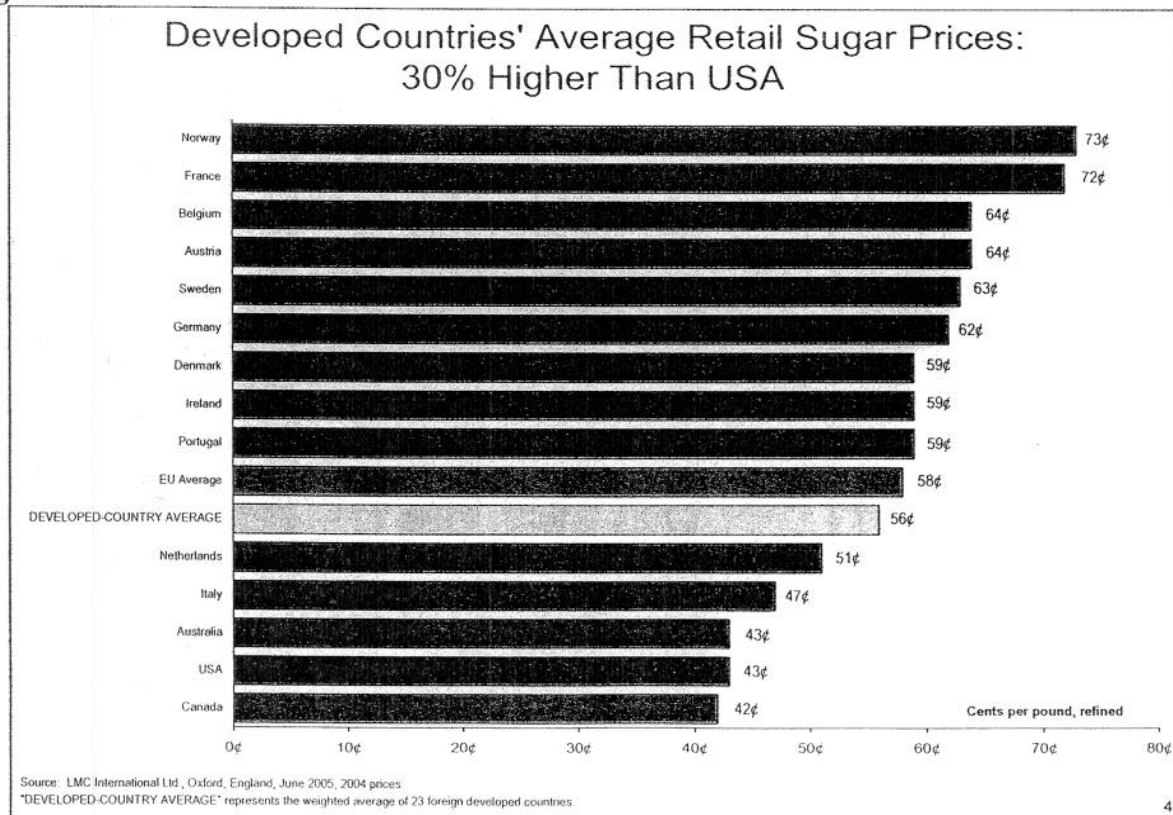


Figure 10

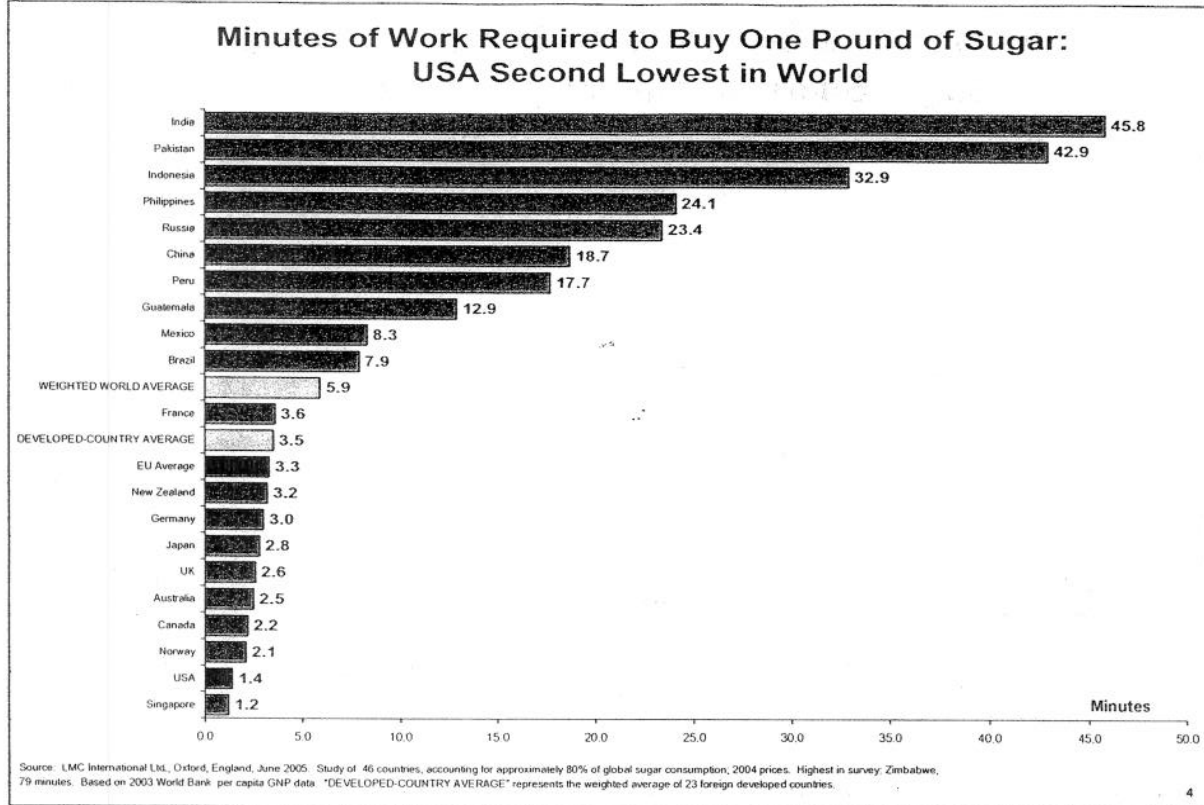


Figure 11

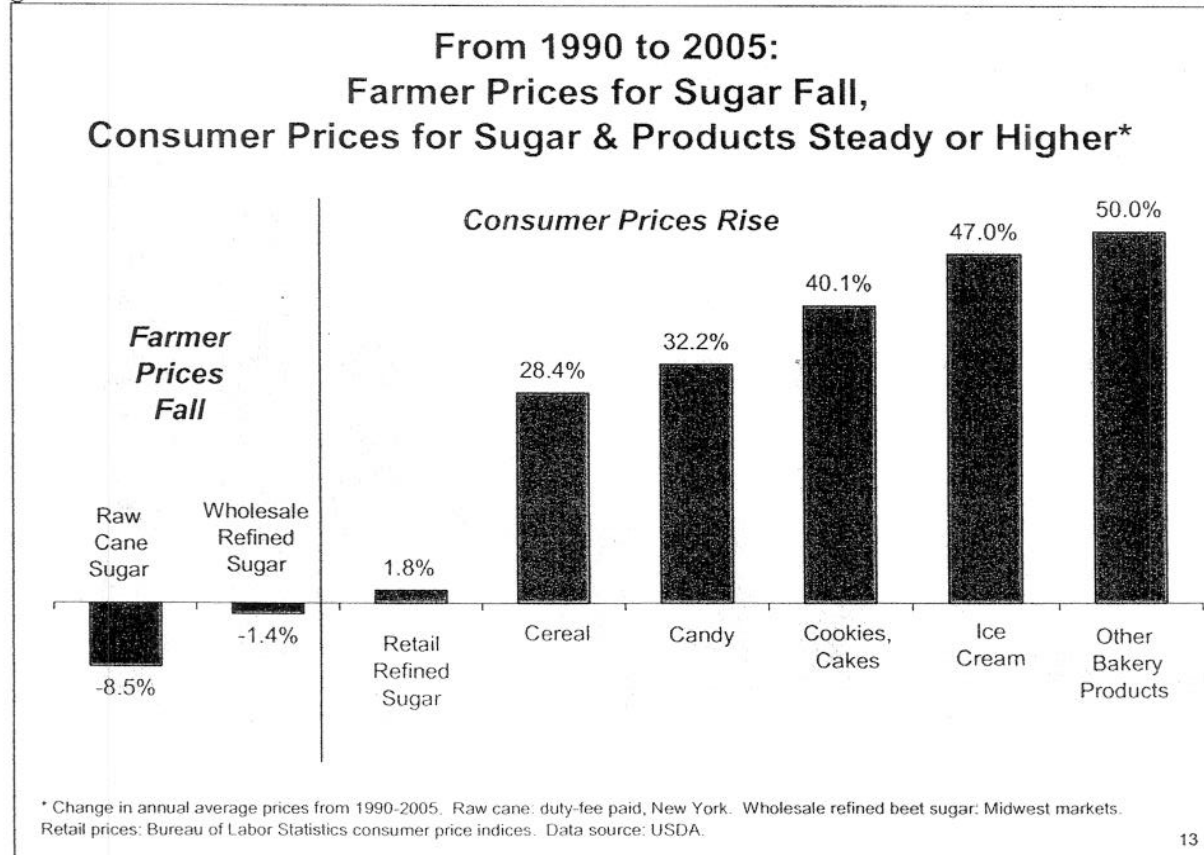


Figure 12

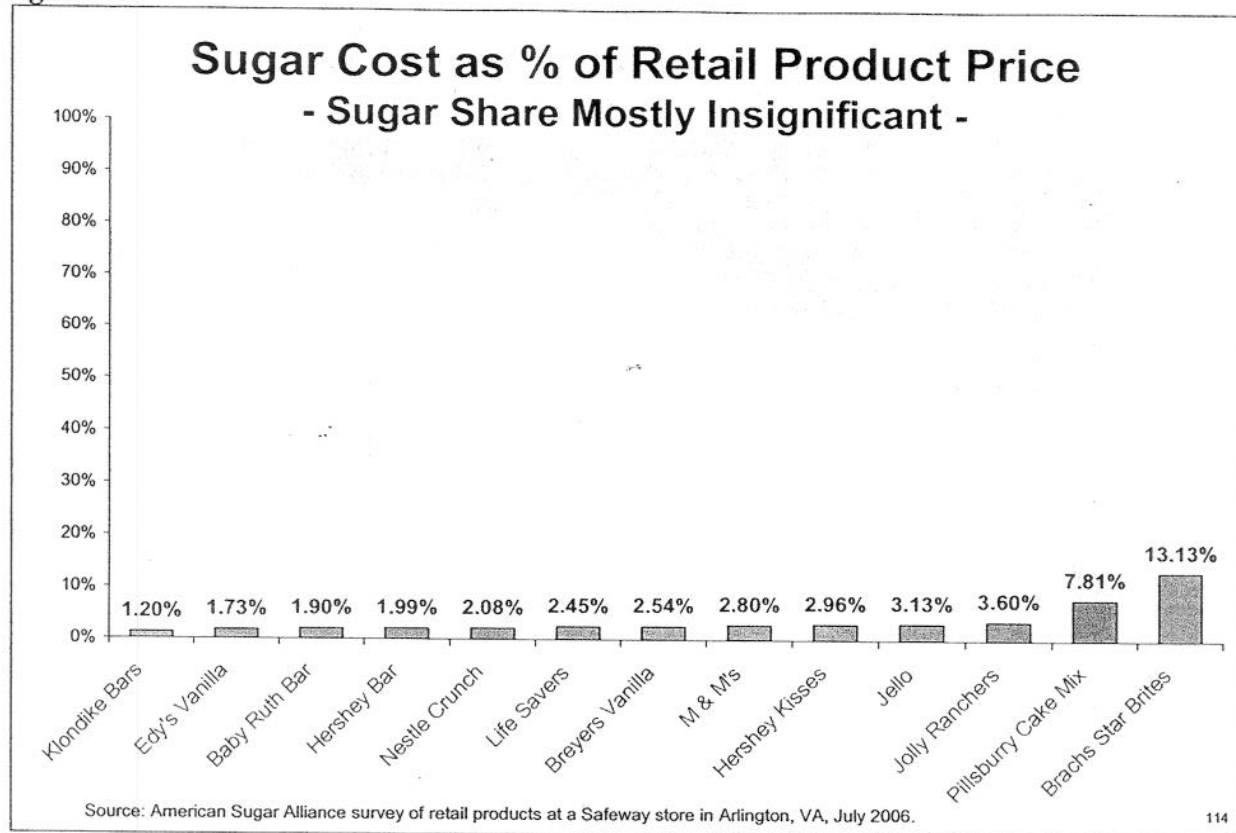
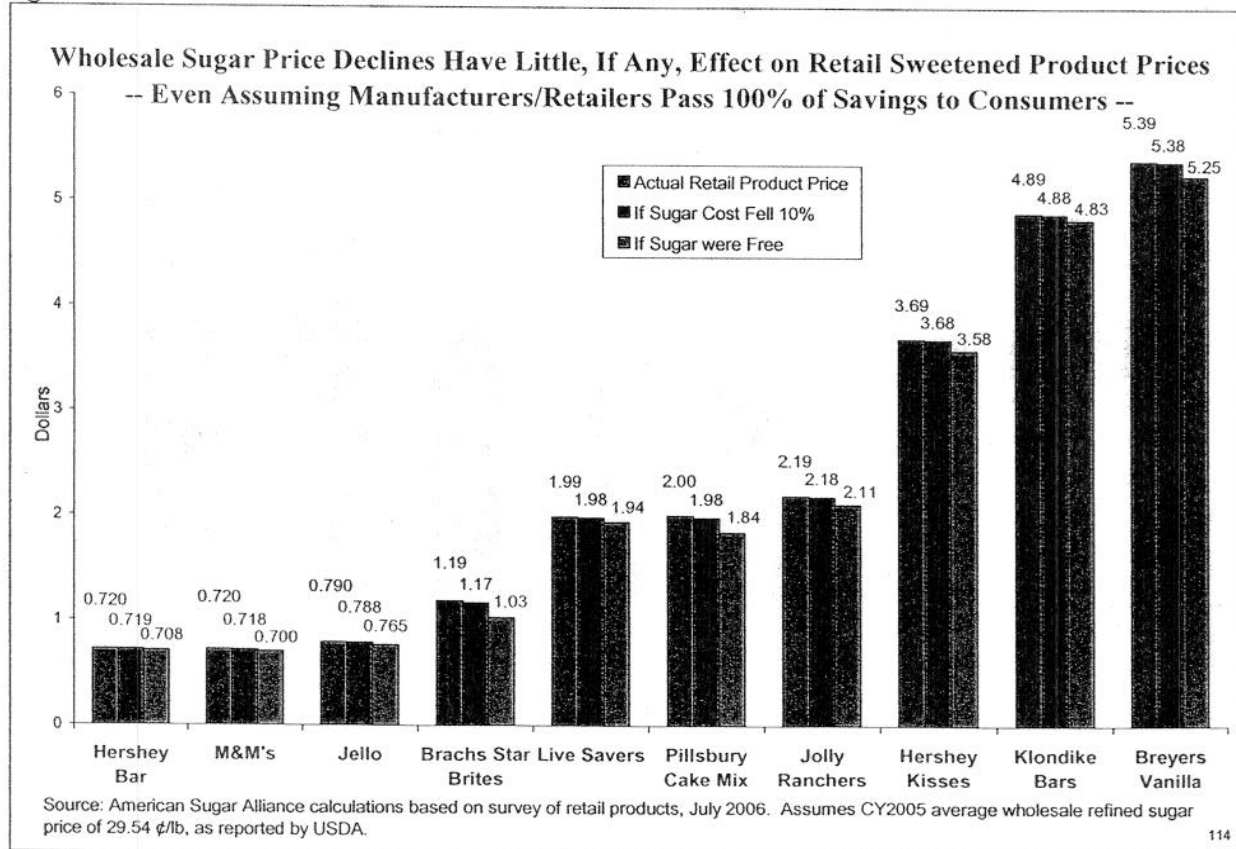


Figure 13



Committee on Agriculture  
U.S. House of Representatives  
Required Witness Disclosure Form

House Rules\* require nongovernmental witnesses to disclose the amount and source of Federal grants received since October 1, 2004.

Name: JACK RONEY  
Address: 2111 Wilson Blvd., St. 600, Arl., VA 22201  
Telephone: 703-351-5055  
Organization you represent (if any): AMERICAN SUGAR ALLIANCE

1. Please list any federal grants or contracts (including subgrants and subcontracts) you have received since October 1, 2004, as well as the source and the amount of each grant or contract. House Rules do **NOT** require disclosure of federal payments to individuals, such as Social Security or Medicare benefits, farm program payments, or assistance to agricultural producers:

Source: \_\_\_\_\_ Amount: \_\_\_\_\_

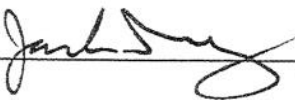
Source: \_\_\_\_\_ Amount: \_\_\_\_\_

2. If you are appearing on behalf of an organization, please list any federal grants or contracts (including subgrants and subcontracts) the organization has received since October 1, 2004, as well as the source and the amount of each grant or contract:

Source: \_\_\_\_\_ Amount: \_\_\_\_\_

Source: \_\_\_\_\_ Amount: \_\_\_\_\_

Please check here if this form is NOT applicable to you: ☒ \_\_\_\_\_

Signature: 

\* Rule XI, clause 2(g)(4) of the U.S. House of Representatives provides: *Each committee shall, to the greatest extent practicable, require witnesses who appear before it to submit in advance written statements of proposed testimony and to limit their initial presentations to the committee to brief summaries thereof. In the case of a witness appearing in a nongovernmental capacity, a written statement of proposed testimony shall include a curriculum vitae and a disclosure of the amount and source (by agency and program) of each Federal grant (or subgrant thereof) or contract (or subcontract thereof) received during the current fiscal year or either of the two previous fiscal years by the witness or by any entity represented by the witness.*

PLEASE ATTACH DISCLOSURE FORM TO EACH COPY OF TESTIMONY.

**Vickie R. Myers**  
Executive Director  
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**Jack Roney**  
Director of Economics  
and Policy Analysis  
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**Phillip W. Hayes**  
Director of Media Relations  
E-mail: [phillipwhayes@aol.com](mailto:phillipwhayes@aol.com)

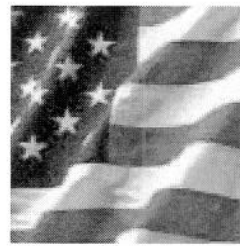


BACKING AMERICA'S BEET AND CANE FARMERS

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***Jack Roney***  
***Director of Economics and Policy Analysis***  
***American Sugar Alliance***

The American Sugar Alliance is the national coalition of growers, processors, and refiners of sugarbeets and sugarcane. Roney has been with ASA since 1996, and represents ASA on matters of domestic and trade policy. Previously, Roney served for seven years as Washington representative for the Hawaiian Sugar Planters Association, and for 15 years with the U.S. Department of Agriculture. Roney earned masters degrees in communications from American University and in international public policy from Johns Hopkins University's School of Advanced International Studies. A native of Bucks County, Pennsylvania, Roney resides in Vienna, Virginia, with his wife, Deborah, and two children, Kyle and Alison.



## **Sugar Issue Brief:**

# **Sugar Subsidy Checks are Unworkable**

August 2006

**AMERICA'S SUGAR PRODUCERS... *Meeting America's Needs***

## Executive Summary

It's not every day that you hear about farmers fighting to *NOT* receive government money.

Most squabbles involving federal farm support have to do with producers looking for additional dollars. But when it comes to sugar, it's the rich food manufacturers who are trying to force government checks down farmers' throats.

For decades, sugar farmers have obtained their incomes from the marketplace instead of relying on government checks, and America's sugar producers want Congress to extend the current supply-management program, which operates at no cost to taxpayers.

On the other hand, some industrial sugar users want to scrap this program in favor of a taxpayer-funded payment program similar to other commodities. Under such a program, sugar prices for farmers would fall and food manufacturers would boost their profits by pocketing the savings.

When you examine this sugar subsidy concept, you quickly realize that multiple problems make it unworkable.

- **Price Tag Problem:** A program shift to sugar subsidy checks would cost taxpayers \$1.3 billion a year—a huge price tag when Congress is staring at a more than \$300 billion annual budget deficit and an \$8 trillion national debt.
- **Political Problem:** A direct payment program for sugar would be nearly impossible to pass, let alone sustain, at a time when farm payments are coming under attack from the Administration, Congressional budget hawks, and well-funded special interest groups. Future budget reconciliation reductions in payments are likely given the current political atmosphere, and such reductions would force sugar producers out of business.
- **Payment Delivery Problem:** The sugar industry is structured differently than other commodities and would need to receive payments in a different manner. An entire infrastructure would need to be built from the ground up, creating added costs and implementation delays.
- **Price Discovery Problem:** A transparent domestic price is cornerstone to a subsidy payment system. Yet there is no publicly traded refined sugar market in the United States, and raw and refined markets do not have a fixed relationship. Grower payments can't be made on price surveys of a spot market from *Milling and Baking News*, a trade publication that currently serves as the main source of wholesale pricing information.
- **Payment Timing Problem:** Payments to producers would have to be made in the second fiscal year after the crop was grown because of time required to process and market sugar (eg. 2005 crop payment made in FY2007).
- **Payment Limit Problem:** Current limits on federal payments—limits that will likely shrink in the upcoming Farm Bill—would send sugar farmers' incomes plummeting.

This would be especially problematic in Louisiana as growers struggle to recover from hurricanes. Furthermore, payment limit realities would encourage producers to restructure their operations in ways that are economically inefficient.

- **Grower Exodus and Refining Capacity Problem:** Sugar subsidy checks are very unpopular among sugar farmers, and if such a system were adopted, farmers would exit the business. Even a small exodus would send shockwaves through the industry because processors and mills are reliant on a steady, constant stream of beets and cane to keep their operations afloat.

Fewer farmers would result in further industry consolidation and would strain an already tight refined sugar capacity. Sugar users depend on America's domestic industry to provide more than 40 different sugars and syrups in hundreds of different packages. They cannot afford the interruptions or headaches that would result from lost capacity.

- **WTO Non-Compliance Problem:** With the international community squarely entrenched against U.S. agricultural subsidies, it makes no sense to scrap a WTO-compliant sugar policy for sugar subsidy checks that could be found illegal in a WTO challenge.
- **Public Perception Problem:** U.S. sugar producers would become the poster child for the anti-subsidy movement if Congress adopted an income support policy for sugar. Such pressure and unpopularity would further bring the long-term sustainability of sugar subsidy checks into question.

If the sugar policy that food manufacturers seem to be favoring were adopted, farmers would lose, taxpayers would lose, America could become dependent on foreign countries for sugar, and grocery shoppers would see no benefit.

Only two groups would win. Industrial sugar users and subsidized Brazilian sugar companies that would likely absorb the market share made available by bankrupted U.S. companies.

Burdening taxpayers, wrecking rural communities that depend on sugar production, and jeopardizing our nation's food security are steep prices to pay so a handful of multinational food companies and foreign sugar superpowers can line their pockets.

That might explain why the American public remains such a strong supporter of the existing sugar policy.

In a recent poll conducted by Harris Interactive, 62% of Americans said Congress should extend the current no-cost U.S. sugar program when they were presented with a choice of policy options. Only 16% favored the income support model being pushed by some sugar users.

Congress should listen to the American people. Congress should extend the proven no-cost sugar policy, not trade it in for an unproven \$1.3 billion train wreck waiting to happen.

## A Pricey Proposal

In a brief prepared for Congress, the Congressional Research Service (CRS) explained that cost would be “a major deterring factor” in transforming the current no-cost sugar policy to an income support program modeled after cotton, soybeans, and grains.

The CRS is correct; the price tag placed on direct payments to sugar producers would be substantial and impractical.

“Total government payouts under a standard program for sugar could exceed \$1.3 billion per year,” according to a June 2006 study prepared by McKeany-Flavell Company, a commodity analysis firm from California that has provided research for more than 70 national and multinational food and beverage companies.

“This would represent a sharp departure from sugar’s long-running status of operating at no net cost to taxpayers,” the study continued.

### Total Sugar Payouts Under Standard Program

Direct Payments	\$ 481,236,000
Counter-Cyclical Payments	\$ 505,036,000
Loan Deficiency Payments	\$ 314,080,000
<b>Total Payments</b>	<b>\$ 1,300,352,000</b>

Source: “The Future of U.S. Sugar Policy,” McKeany-Flavell Company,  
Oakland, California, June 14, 2006.

In today’s budget atmosphere, this cost hurdle likely would be too steep to overcome. Unlike the 2002 Farm Bill, which was negotiated during a time of budget surpluses, the 2007 Farm Bill debate is taking place amidst budget deficits.

According to the Congressional Budget Office, the federal government spent \$319 billion more than it took in during FY2005. And, in the first eight months of FY2006, the federal government had already incurred a deficit of \$223 billion.

### How much money is \$1,300,000,000?

\$1,300,000,000 would pay the salaries of 45,236 enlistees for the War on Terror.

\$1,300,000,000 is enough to hire 49,328 new border patrolmen.

\$1,300,000,000 equals the annual pay of 28,020 public school teachers.

\$1,300,000,000 could send 107,198 underprivileged students to a public university for a year.

\$1,300,000,000 would cost taxpayers \$108,333,333 every month; \$25,000,000 every week;  
\$3,561,644 every day; \$148,317 every hour; and \$2,472 every minute.

## Where Would the Money Come From?

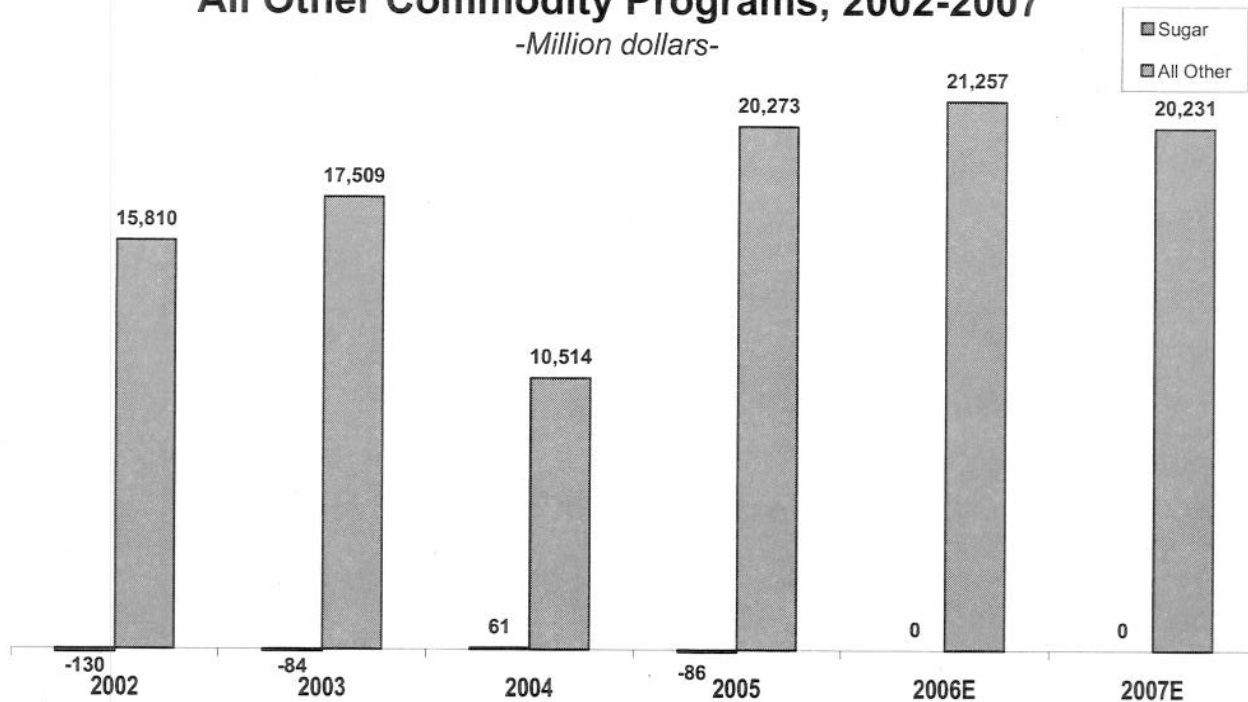
Staggering deficit figures, combined with the country's ongoing obligations in the War on Terror and hurricane recovery, make it highly unlikely that any new money will be made available to fund sugar subsidy payments.

Existing federal programs would have to be reduced as offsets to free up money for sugar payments, and the federal agricultural budget would be the expected target.

That could be tragic for non-sugar farmers, considering that the estimated \$1.3 billion needed to fund a revamped sugar program would equal 8% of the average annual farm payments made to all commodities from 2002 to 2005. In other words, farmers could expect to see an 8% decrease in their federal farm payments to fund this type of sugar policy approach.

## Government Net Outlays for Sugar and All Other Commodity Programs, 2002-2007

-Million dollars-



Data source: USDA/FSA, February 2006. Negative figures = net revenues.

## Why Transition When Farm Subsidies Are Under Attack?

Compounding the problem for proponents of a sugar subsidy program is the fact that agricultural spending in general has come under heavy fire.

In the FY2007 budget proposal that President Bush sent Congress, he requested that all crop payments to farmers be lowered by 5%. The White House has also pledged to the World Trade Organization (WTO) that it would be willing to curb farm spending by 60%.

It is highly unlikely that an Administration bent on cost-cutting in Rural America would look favorably on a \$1.3 billion sugar program. Such opposition would make passage nearly impossible.

**Farm subsidy payments will undoubtedly be the target of an aggressive and well-funded lobbying effort—this is not the atmosphere to make a pricey sugar policy transition from no cost to subsidy checks.**

Not to mention, there are powerful lobbying groups looking to send current farm spending levels spiraling. From foreign countries, to environmental groups, to think tanks, opponents of farm subsidies are more optimistic than ever that agricultural spending will be reduced in the 2007 Farm Bill.

A front-page article in the March 14, 2006 edition of *The Wall Street Journal* summed it up by saying, “The current anti-subsidy sentiment, rising over the last year in the U.S., is stirring attention because it is unusually broad...Participants include Oxfam and Environmental Defense from the left, the National Taxpayers Union on the right and the libertarian Cato Institute. Prominent philanthropic organizations, including the William and Flora Hewlett Foundation, are financing some of this advocacy.”

Farm subsidy payments will undoubtedly be the target of an aggressive and well-funded lobbying effort—this is not the atmosphere to make a pricey sugar policy transition from no cost to subsidy checks.

### **Could Subsidy Checks Provide the Same Income Stability?**

Given the widespread desire to curtail agricultural dollars and the uncertainty surrounding the fate of U.S. farm subsidies in WTO negotiations, political uncertainties would provide farmers with very few assurances that an income support program would provide the stability they need to make long-term business decisions.

This fact is very troubling to the banking community that lends farmers the money needed to produce their sugar crops and keep their farming operations afloat.



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July 26, 2006

The Honorable Saxby Chambliss, Chairman  
 Committee on Agriculture, Nutrition and Forestry  
 U. S. Senate  
 328A Russell Senate Building  
 Washington, D.C. 20510

Dear Mr. Chairman:

First South Farm Credit is the Farm Credit System's largest agricultural and agribusiness production lender in Louisiana, Alabama, and Mississippi. With approximately \$1 billion in assets First South has 47 offices serving the agricultural communities in these three states. Our financial institution has provided uninterrupted and successful agricultural credit and financial services to farmers, agricultural producers and agribusiness for over 75 years.

First South joins the commercial bankers, as well as other financial institutions, in voicing a concern that efforts may be underway to reform current sugar policy in the upcoming Farm Bill. First South has a stake in how federal farm policy is processed, especially when it involves the stability of the Louisiana sugar industry. Approximately thirty percent (30%) of the First South loan portfolio in Louisiana is in sugarcane and sugar related businesses. Our financial institution, as well as other institutions, depends on stabilized sugar policy in order to provide viable financing options for sugar growers, sugar mills and other sugar-related businesses in South Louisiana.

The sugar business is unique to this area of our country and cannot be replaced by another commodity. We cannot allow the uncertainties in trade policy and the reluctance to continue federal spending on agriculture to steer us away from a proven sugar program. South Louisiana is economically dependent on sugar and cannot withstand an unproven change in sugar policy that would continue to add to the economic devastation along with hurricanes Katrina and Rita.

We thank you for your consideration as we move forward with Farm Bill hearings.

Sincerely

Stephen L. Rochelle  
 President and CEO

Cecil Corbello  
 Louisiana Division President

Sells J. Newman  
 Senior Vice President  
 Legislative Affairs

/cs

First South Farm Credit, ACA

*Serving agriculture in Alabama, Louisiana, Mississippi and part of Tennessee*

## Implementation Headaches

As the old saying goes, the devil's in the details. This certainly applies to sugar policy options.

In the unlikely scenario that money were no object and Congress were willing to spend \$1.3 billion to fund a shift from a no-cost program to sugar subsidy checks, there would still be major implementation hurdles. That's because sugar is fundamentally different than other commodities and the transfer of subsidy checks would therefore have to be different.

Unlike growers of rice or soybeans, sugar farmers cannot go to a world market to sell their crop. Sugarbeets and sugarcane are worthless until they are turned into sugar by sugarbeet factories and sugarcane mills.

And unlike farmers of corn or wheat, sugar growers don't deal with local USDA Farm Service Agency (FSA) offices or take out loans from the government. The mills and the processors instead deal with the U.S. Department of Agriculture and take out non-recourse loans.

### Who Would Receive the Payments?

The question now becomes who would receive the sugar subsidy checks and how would those checks be distributed by the FSA?

If subsidy checks went directly to sugar farmers—as they do for other commodities—an entire infrastructure would need to be built from the ground up, creating added costs and implementation delays.

***If subsidy checks went directly to sugar farmers—as they do for other commodities—an entire infrastructure would need to be built from the ground up, creating added costs and implementation delays.***

Cane mills that are not cooperatively owned by farmers would likely receive nothing if payments went directly to farmers. When prices drop—as they would under a sugar subsidy program—mills feel the pain as much as farmers. Factories would close if mills were excluded from federal subsidy supports, leaving cane growers without a place to process their crop.

If payments instead went directly to processors and mills to disperse to growers, then a new set of problems arise. Sugar companies would become large recipients of federal agricultural subsidies and would immediately be targeted as corporate welfare beneficiaries. This would increase political pressures on the sugar industry and would create an atmosphere where sugar companies were forced to constantly defend a subsidy system that they never wanted.

In addition, this setup could lead to bickering between farmers and processors. Would mills and beet processing facilities pass along all of the federal payments to growers, or would there be administrative fees taken off the top? If fees were taken off the top, how much would be considered appropriate?

## How Would Payments be Distributed?

Further complicating the headaches of implementing sugar subsidies is an overworked and underfunded FSA system that would be charged with figuring out how to deliver subsidy checks to farmers.

In a March 9, 2006 hearing before the House Appropriations Subcommittee on Agriculture, FSA Administrator Teresa Lasseter outlined the many challenges currently facing the agency.

Among them: The added burden of distributing hurricane and other disaster assistance; the costly delivery of tobacco buyout payments; a severely antiquated computer system and technology infrastructure; staff that needs better training; an inability to hire additional employees or contractors to handle an ever increasing workload; and a budget that has not increased fast enough to cover basic operational costs.

“The time has passed, however, when we can promise to do more with less. The time has come when we must make some difficult choices,” Lasseter told lawmakers about the agency’s challenges.

Compounding these operational problems, the USDA was looking to downsize and close 713 local FSA offices—188 offices of which were from sugar-producing states.

Because of outcry from farm state legislators, plans for closure were temporarily halted in October 2005. Future closures, however, have not been ruled out as the USDA is continuing its quest to trim overhead costs.

If no-cost sugar policy gets a facelift and FSA has to decide how to administer sugar subsidy payments, Lasseter and her staff will be asked to do more with less—something the agency has admitted it is ill equipped to do.

### Number of FSA Offices in Sugar States That Were Targeted for Closure

<u>State</u>	<u>Total FSA Offices</u>	<u>Targeted for Closure</u>	<u>% of Total</u>
California	32	6	19%
Florida	36	11	31%
Idaho	35	12	34%
Louisiana	42	15	36%
Michigan	51	12	24%
Minnesota	79	22	28%
Montana	49	6	12%
Nebraska	81	23	28%
North Dakota	52	6	12%
Oregon	25	4	16%
Texas	206	70	34%
Washington	26	1	4%
<b>TOTAL</b>	<b>714</b>	<b>188</b>	<b>26%</b>

Source: USDA

## Payment Limits Cloud the Picture

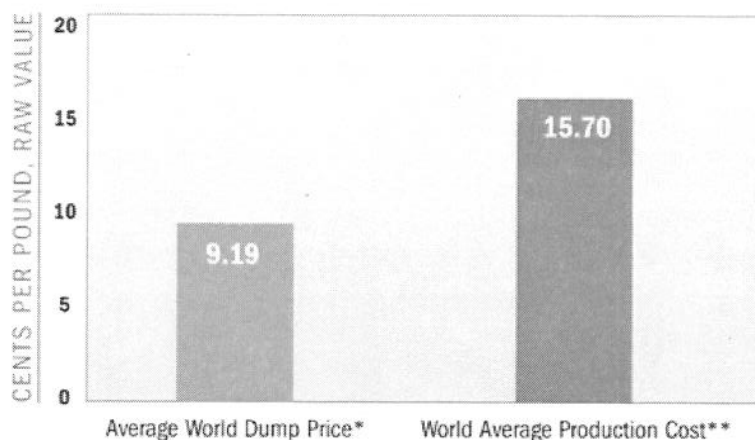
Sugar is also unique in that it is one of the only farm commodities in the world that does not have a true world market. That's because 80% of the sugar grown around the world is never traded on an open market—it's sold in the country where it's grown for prices similar to U.S. prices.

The other 20% is unreliable surplus sugar that is dumped onto a thinly traded market for any price it will bring. This sugar is so heavily subsidized in its home market that it can be sold on a world dump market at prices below the cost of production.

The world dump market for sugar is the most volatile agricultural commodity market in the world, prone to major peaks and valleys. Since the 1970s, prices on this dump market have ranged from 3 cents a pound to more than 60 cents a pound.

### World Sugar Dump Market Price

Barely More Than Half the World Average Cost of Producing Sugar  
(20-Year Average, 1983/84 - 2002/03)



\* New York contract #11, f.o.b. Caribbean ports. Source: USDA.

\*\* Beet and cane sugar weighted average, raw value. Source: "The LMC Worldwide Survey of Sugar and HFCS Production Costs: The 2003 Report," LMC International, Ltd., Oxford, England, December 2003.

Considering the bulk of farm subsidy payments are calculated by taking the difference between a world price and a commodity's target price (set by the government), rock-bottom prices on the world dump market for sugar become very problematic. Compounding this problem is the fact that there is no publicly traded refined sugar market in the United States, and raw and refined markets do not have a fixed relationship.

The gap between a sugar producer's current government loan rate and the price valleys of the dump market could make sugar payments astronomical—far higher than the payments per farm allowed in the other farm programs. Federally mandated payment limits on farm subsidy payments would quickly become an issue for sugar farmers.

### How Soon Would Sugar Producers Hit the Limit?

Sugar farmers would hit payment limits on their first 3 cents per pound of direct payments on about 200 acres of sugarbeets or 170 acres of sugarcane.

In other words, payment limits would be an issue for almost every sugar farmer in America, and that's assuming that these growers are not already nearing or hitting payment limits on other crops.

As farms have grown to achieve greater efficiency and lower production costs, they have also become more diversified. Farmers plant a wide array of crops to hedge against extreme price fluctuations in a single crop.

For this reason, most beet farmers already receive government payments on corn, barley, wheat, and other commodities they grow. Some cane growers produce rice, cotton, and soybeans, which also involve payments.

Unless sugar subsidies received their own separate payment limit cap—an idea that would be widely unpopular with other commodities—the payments sugar farmers see from other crops would drive down the amount of income support they could receive on their sugar crops.

### **What Do Payment Limits Mean to Farmers?**

Lost income caused by payment limits is a major hurdle to the viability of an income support program for sugar, according to the study conducted by McKeany-Flavell.

That study stated: "Limits on the program payments each farm can receive could make a large portion of these payments unavailable to sugar producers. Coupled with lower market prices, these limits would significantly reduce farm incomes in the sugar-producing sector."

Such a drop in income would be especially devastating in Louisiana and Florida where farmers are struggling to recover after the 2005 hurricanes. McKeany-Flavell estimates that losses due to payment limits could cost Florida sugar farmers \$263 million a year and Louisiana sugar farmers \$287 million annually.

#### **Standard Program: Farm Income Effects**

<b>Cane</b>	<b>% of total acreage</b>	<b>Loss due to payment limitations (\$ million)</b>
Florida	45%	263.4
Louisiana	49%	286.8
Texas	5%	29.3
Hawaii	1%	5.9
<b>Total</b>		<b>585.4</b>

Source: "The Future of U.S. Sugar Policy," McKeany-Flavell Company,  
Oakland, California, June 14, 2006.

These losses would severely jeopardize the future of the Louisiana sugar industry, which has been in existence for more than 200 years, because soil and weather conditions in southern Louisiana leave farmers few crop options to replace sugarcane.

As Jessie Breaux, a farmer from Franklin, Louisiana said of the situation, “Do away with our current sugar policy and the only thing we’ll grow in south Louisiana is our unemployment rate.”

Besides lost income, the McKeany-Flavell study also suggests that the issue of payment limits could actually reverse the business efficiencies that sugar farmers have gained over the past few decades.

“When payment limitations are taken into account, farmers may be compelled to restructure their operations in order to continue producing a crop,” read the study. “This could include breaking up farms into smaller units in order to stay under the payment limit. Such a move could cause inefficiencies in crop production, from management and administrative tasks to the actual production of the crop.”

### **What Does the Future Hold for Payment Limits?**

The issue of payment limits is further muddled by the fact that Congress is under tremendous pressure to lower the payment cap in the upcoming 2007 Farm Bill.

In its last two budget recommendations, the White House has asked Congress to reduce by 30% the cap on payments a single farm can receive from the government. And following a series of hearings across the country, the USDA has signaled that it will push for stricter payment caps in the upcoming Farm Bill debate.

Furthermore, a prominent member of the Senate Agriculture and Budget Committees has led a charge in seeking a tighter cap on farm payments. This lawmaker has proposed numerous amendments on the subject since the 2002 Farm Bill. He has introduced a bill, which has eight co-sponsors, to lower limits in the 109<sup>th</sup> Congress. And, he is expected to be even more energized as Farm Bill reauthorization talks unfold.

A Commission on the Application of Payment Limitations for Agriculture was even formed as part of the 2002 Farm Bill to examine the issue of reducing farm subsidy caps. The Commission found that “any substantial changes should take place with reauthorization of the next [2007] Farm Bill.”

***In today’s political atmosphere, it is very likely that farm payment limits will shrink, making the financial picture even bleaker for America’s sugar farmers if a sugar subsidy program were enacted.***

That’s exactly what farm program opponents such as the powerful Environmental Working Group expect to happen. These groups are more organized, more motivated, and more free-spending than ever, and they will focus all of their attentions on tightening the reigns on agricultural spending in a Farm Bill reauthorization.

In today’s political atmosphere, it is very likely that farm payment limits will shrink, making the financial picture even bleaker for America’s sugar farmers if a sugar subsidy program were enacted.

## The Chain Reaction Could Crumble an Industry

Scrapping the current no-cost sugar policy in favor of an income support program is very unpopular among sugar farmers. These growers count on the stability of the current program and often depend on sugarbeets and sugarcane to help support less-profitable farming operations.

If a transition were made to an unproven subsidy check system, which would lower farmer incomes, the American Sugar Alliance expects numerous farmers to exit the sugar-growing business.

And because of the unique costs associated with sugar farming, such as special farming equipment and having to buy shares of beet processing cooperatives, the American Sugar Alliance would not expect new farmers to replace exiting sugar growers.

Even a minor exodus from sugar farming could set off a chain reaction that reverberates across the entire industry because processors are so dependent on farmers to supply the crops they need to run their operations.

Sugar prices were so low from 1996 to 2004 (down 20%) that even the most efficient beet processors and cane mills had to achieve higher levels of efficiency to stay in business.

This meant investments to improve yields in the fields, new technologies to streamline processing facilities, and increasing throughput in the factories.

Every time a farmer goes out of business, the factory he or she grew for has fewer beets to slice or less cane to crush. This decreases throughput, decreases efficiency, and decreases company profits.

If enough throughput is lost, the industry would see widespread beet factory and cane mill closures and a tightening of America's sugar processing capacity. And with 33 closures since 1996, U.S. food manufacturers cannot afford the capacity problems that would arise with additional closures.

### Who Would Replace America's Lost Sugar Production?

"If this conclusion is realized, domestic production in future years could be jeopardized, creating further dependence on foreign sugar," found McKeany-Flavell in their recent study on transforming no-cost sugar policy to a subsidy check system.

### **Foreign Sugar and America**

***Once upon a time, America learned a sour lesson about relying on others for food.***

**1942:** Dependence on foreign sugar led to sugar rationing during World War II.

**1962:** The Cuban embargo sent U.S. food manufacturers scrambling for sugar.

***But America figured it out: Feeding ourselves is the first rule of national security.***

**1982:** Congress created a sugar policy that gave America a reasonably priced, homegrown alternative to unreliable foreign sugar supplies.

**2002:** Congress mandated that sugar policy wouldn't cost taxpayers a dime.

***Unproven sugar subsidy checks would put America on a path back to food insecurity.***

“Just as we are experiencing problems with our dependence on foreign oil, sugar users would have many obstacles to overcome, including sugar quality, consistency, packaging, and the ability of suppliers to make just-in-time deliveries,” read the study.

Domestic sugar supply shortages caused by hurricanes in 2005 spotlighted the problems U.S. food manufacturers would face if they had to rely solely on foreign sugar suppliers.

Refined sugar coming from Mexico contained metal shavings and had to be re-refined by U.S. companies—this added costs and delayed deliveries. Unlike U.S. sugar that is delivered by rail or trucks, foreign refined sugar brought in after the hurricanes arrived in various sized tote bags, which U.S. food manufacturers were not equipped to receive.

In addition, foreign sugar must be shipped on barges in very large quantities. U.S. producers, by contrast, run just-in-time delivery schedules. That way, food manufacturers can get an exact amount of sugar when they need it, thus avoiding storage costs.

These headaches help explain why industrial sugar users have become more supportive of a strong, domestic sugar industry.

“Apparently stung by bad experiences with sugar imports after Hurricane Katrina reduced U.S. sugar production in Louisiana, the Sweetener Users Association softened its opposition May 10 to the U.S. sugar program,” the *National Journal* wrote about the situation following a May Senate Agriculture Committee hearing on sugar policy.

At that hearing, a longtime sugar policy opponent who works for The Hershey Company testified, “As sugar users, we want and need strong and healthy sugar production and processing. We believe it is in our interest to have a geographically diverse production base in the United States for both sugar beets and sugar cane.”

### 33 Sugar Mill and Refinery Closures Since 1996

#### BEET CLOSURES

Spreckels Sugar, Manteca  
California, 1996

Holly Sugar, Hamilton City  
California, 1996

Western Sugar, Mitchell  
Nebraska, 1996

Great Lakes Sugar, Fremont  
Ohio, 1996

Holly Sugar, Hereford  
Texas, 1998

Holly Sugar, Tracy  
California, 2000

Holly Sugar, Woodland  
California, 2000

Western Sugar, Bayard  
Nebraska, 2002

Pacific Northwest, Moses Lake  
Washington, 2003

Western Sugar, Greeley  
Colorado, 2003

Amalgamated Sugar, Nyssa  
Oregon, 2005\*\*

Michigan Sugar, Carrollton  
Michigan, 2005\*\*

#### CANE CLOSURES

Ka'u Agribusiness  
Hawaii, 1996

Waialua Sugar  
Hawaii, 1996

McBryde Sugar  
Hawaii, 1996

Breaux Bridge Sugar  
Louisiana, 1998

Pioneer Mill Company  
Hawaii, 1999

Talisman Sugar Company  
Florida, 1999

Amfac Sugar, Kekaha  
Hawaii, 2000

Amfac Sugar, Lihue  
Hawaii, 2000

Hawaiian Commercial & Sugar, Paia  
Hawaii, 2000

#### CANE REFINERY CLOSURES

Aiea, C & H  
Hawaii, 1996

Everglades, Imperial  
Florida, 1999

Evan Hall Sugar  
Cooperative  
Louisiana, 2001  
Caldwell Sugar  
Cooperative  
Louisiana, 2001  
Glenwood Sugar  
Cooperative Louisiana,  
2003  
New Iberia Sugar  
Cooperative  
Louisiana, 2005  
Jeanerette Sugar  
Company Louisiana,  
2005

U.S. Sugar, Bryant  
Florida, 2005\*

Cinclare Central Facility  
Louisiana, 2005\*  
Atlantic Sugar, Belle  
Glade  
Florida, 2005\*\*

Sugarland, Imperial  
Texas, 2003

Brooklyn, Domino  
New York, 2004

\*Phasing out operations, 2005-07. \*\*Suspended operations for 2005/06.

Note: In 2006, 23 beet factories, 19 raw cane mills, and 8 cane refineries remain in continuous operation, a 39% drop since 1996.

American Sugar Alliance, March 2006.

7

## International Trade Implications

Even though America would become more dependent on foreign sugar under a federal income support program, the country's sugar producers would come under much more scrutiny in the international trade arena.

The current U.S. sugar program has never been formally challenged in a WTO court for legality. This is in stark contrast to America's income support farm programs, which have come under fire from other countries.

### Why Change Sugar Policy in this Atmosphere?

Last year, WTO appellate panels ruled against the U.S. and European Union in cases brought by Brazil about the legality of U.S. cotton subsidies and EU sugar subsidies.

***With the international community squarely entrenched against U.S. agricultural subsidies, it makes no sense to scrap a WTO-compliant sugar policy for sugar subsidy checks that could be found illegal in a WTO challenge.***

Congress was forced to quickly alter the U.S. cotton program to avoid potential WTO-sanctioned retaliatory measures against American agricultural products. And, the EU is implementing a major sugar policy reform that will bankrupt a large share of its sugar growers.

America's problems are not solely limited to the cotton program. In a report prepared for Congress, CRS acknowledged, "Additional permanent modifications to U.S. farm programs may still be needed to fully comply with the 'actionable subsidies' portion of the WTO ruling."

That's because other U.S. commodities operate in a direct payment system that is being questioned by the WTO. Brazil has hinted that the U.S. wheat, corn, and soybean programs may be in the crosshairs soon because of the trade-distorting nature of some subsidy payments.

With the international community squarely entrenched against U.S. agricultural subsidies, it makes no sense to scrap a WTO-compliant sugar policy for sugar subsidy checks that could be found illegal in a WTO challenge.

### Would Sugar Subsidy Checks Increase America's AMS?

Some who have advocated for a switch from the current sugar program to subsidy checks have used America's Aggregate Measure of Support (AMS) as a reason.

The AMS is the term used by the WTO to refer to a country's total level of agricultural subsidization. It is a calculation based on government payments to growers and other policies, such as price supports.

Even though sugar farmers do not receive subsidy checks, the WTO calculates that the current sugar program counts \$1 billion against America's AMS because U.S. sugar prices are higher than prices on the world dump market.

America is bound by WTO rules to have a total AMS of no more than \$19.1 billion, and the country is currently bumping up against this ceiling. Proponents of overhauling sugar policy had claimed that America's AMS could be lowered if the current sugar program were replaced with sugar subsidy checks.

However, the researchers at McKeany-Flavell believe this assumption is false. Those researchers predict that sugar's share of the AMS would likely grow to \$1.3 billion under a direct payment program.

## Public Enemy Number One

Ask the average person on the street to explain the AMS, and you'd get a lot of blank stares. But ask the average person to explain farm subsidies, and you'd evoke a wealth of responses.

Unfortunately for farmers, most of those responses would be negative and would likely include the misperception that "farmers get paid not to grow."

America is two—going on three—generations removed from the farm, and the general public has little sympathy for federal farm payments.

This dislike for farm subsidies is only perpetuated by the nation's news media. An examination of the country's top newspapers showed that 19 of the top 20 publications have actively editorialized against the subsidy payment program.

Some farm policy supporters will shrug this off as Big City media being biased against Rural America.

However, it is never wise to pick a fight with anyone who buys ink by the barrel, and those 19 papers reach 18.2 million readers on a daily basis.

### Would Sugar Inherit a Worse Image?

If the current no-cost sugar program were replaced with a subsidy check system, the sugar industry would have to deal constantly with this public image nightmare. And it's not like the sugar industry is a media darling now, so subsidy checks would only deepen public scorn.



### Farm Subsidy Headlines on America's Editorial Pages

**USA Today** January 14, 2002

"Congress fails to wean farms off taxpayer funds"

**The Wall Street Journal** February 1, 2002

"Prairie Plutocrats"

**The New York Times** Nov. 10, 2003

"Welfare Reform for Farmers"

**Los Angeles Times** October 10, 2001

"Lean Times, Fat Farm Bill"

**The Washington Post** July 21, 2006

"Farm Harm"

**Chicago Tribune** February 25, 2002

"Farming for billions"

**The Philadelphia Inquirer** May 10, 2002

"Congress' worst in new farm bill"

**The Houston Chronicle** January 2, 2002

"Farm Subsidies:

Costly government program hopelessly out of control"

**New York Post** May 26, 2002

"Washington's Feeding Frenzy"

**Dallas Morning News** May 2, 2002

"Farm bill: House-Senate pact perpetuates rotten system"

**New Jersey Star Ledger** March 18, 2005

"Put agribusiness on a diet"

**Atlanta Journal-Constitution** July 3, 2005

"Farm subsidies an unfair deal"

**Arizona Republic** May 23, 2002

"Welfare by the Bushel, But Not for Single Moms"

**New York Newsday** February 21, 2002

"U.S. Farm Subsidies Should Be Cut, Not Expanded"

**San Francisco Chronicle** March 20, 2002

"Farming for dollars"

In fact, the American Sugar Alliance would anticipate that sugar producers would become the poster child for the anti-ag-subsidy movement if an income support model were adopted. That's because processors and mills would have to be included in the subsidy payment program in order to survive absent the current sugar policy.

Large payments would go to companies, and the largest companies would obviously receive the heftiest payouts. "Big Sugar" would become "King Sugar" overnight, replacing "King Cotton" atop the subsidy-payment hit list.

The fact that all beet companies and many cane companies are cooperatively owned by farmers would make no difference in the court of public debate. Just look at Riceland Foods, a cooperative owned by rice farmers, which is held up by farm policy opponents as the nation's largest subsidy recipient and the embodiment of corporate welfare.

Under a sugar income support program, sugar companies would most likely supplant Riceland as America's biggest subsidy recipient. For a preview of what sugar farmers would have to look forward to, here's an excerpt from a 2004 article entitled "Farm Subsidies vs. National Security," written by a Heritage Foundation fellow:

"American cities still lack the resources to prevent a catastrophic terrorist attack. And Washington sends \$110 million in farm subsidies to an Arkansas co-op named Riceland Foods.

"Many troops risking their lives in Afghanistan and Iraq lack the necessary equipment to protect themselves, such as body and vehicle armor. And several members of Congress vote themselves farm subsidies as much as 119 times larger than what the typical farmer receives.

"Millions of overtaxed Americans live paycheck to paycheck. And Washington doles out these tax dollars to David Rockefeller, Ted Turner, basketball star Scottie Pippen and former Enron CEO Ken Lay.

"This year, Washington will spend more on corporate welfare than on homeland security.

"What's going on?

"It gets worse: 78 farms received more than \$1 million each in subsidies in 2002. The \$110 million received by Riceland Foods that year was more than Washington gave to every farmer in 12 states combined. Their subsidy alone could have funded seven Blackhawk helicopters, 1,200 airport luggage scanners or an additional 1,700 border patrol agents."

This damning article was distributed nationally on the Knight-Ridder Tribune wire, a service that reaches 1,000 newspapers, TV, and online services from coast to coast. Why would sugar farmers want this kind of negative attention?

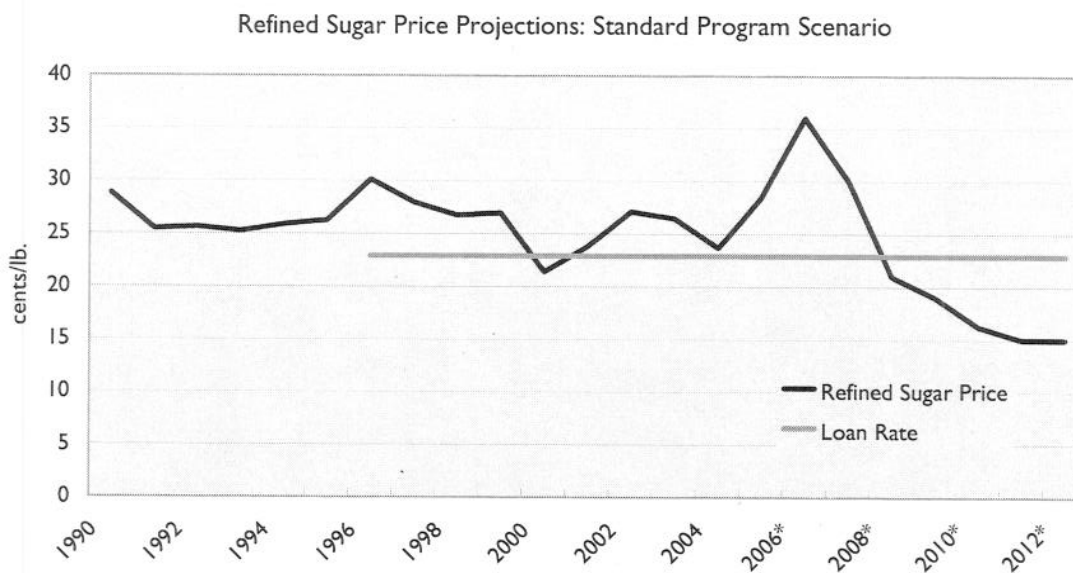
## Only Two Winners with Sugar Subsidies

One of the oddest things about the sugar subsidy situation is the fact that the sugar producers who would have to defend the possible plan on Capitol Hill and face the wrath of public scrutiny never asked for the program.

On the other hand, the beneficiaries of an income support program for sugar could reap the rewards without the headache of taking public fire since they would not directly receive the subsidies. Those beneficiaries include just two groups, industrial sugar users and Brazil.

### How Would Food Manufacturers Win?

McKeany-Flavell predicts that refined sugar prices would fall far below the break-even point (the government loan rate) for domestic sugar producers. This drop would translate into cheaper ingredient prices for manufacturers of candy, cakes, ice cream, and other sweetened products.



Source: "The Future of U.S. Sugar Policy," McKeany-Flavell Company, Oakland, California, June 14, 2006.

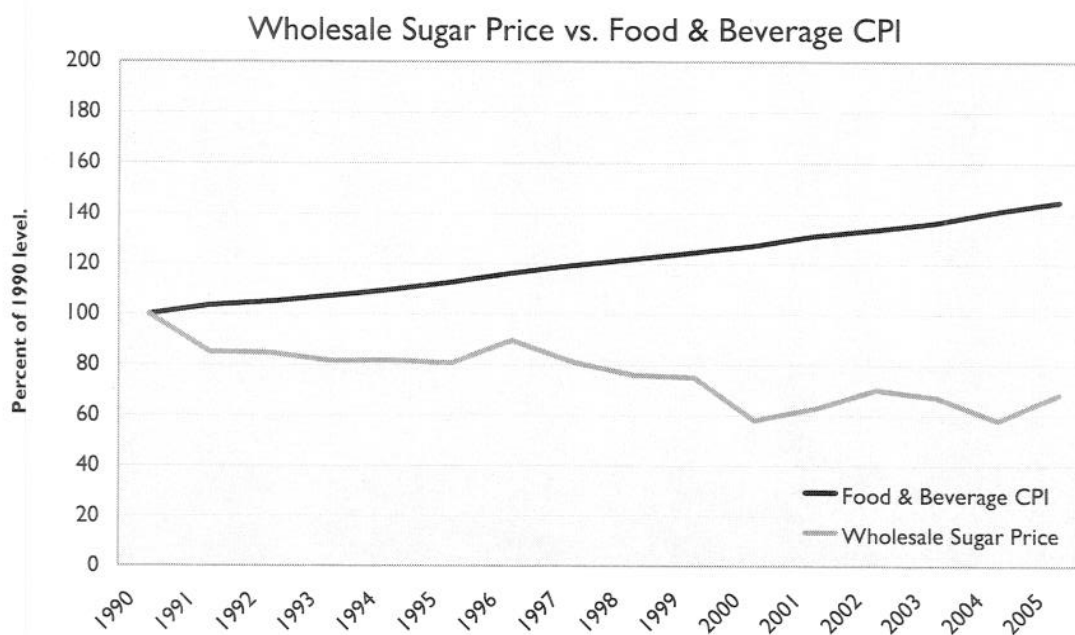
### Would Lower Prices for Sugar Mean Lower Prices for Shoppers?

Rest assured that large food manufacturers are not spending so much time and money on lobbying for cheaper sugar prices so they could pass the savings along to grocery shoppers. Food manufacturers are spending so much time and money on lobbying for cheaper sugar prices so they can boost their profits.

Among the findings in the McKeany-Flavell study: "Consumers would see little or no benefit from lower sugar prices, as food manufacturers historically have not passed savings from lower input costs along to consumers."

This lack of pass through has been very evident since 1990, as sugar prices have dropped but prices for sweetened goods have steadily risen.

The price food manufacturers pay for sugar fell by 1.4% from 1990-2005, according to the USDA. Over the same period, data kept by the Bureau of Labor Statistics show that the price for candy rose 32.2%, the price for ice cream rose 40.1%, the price for cookies and cakes rose 47%, and the price of other bakery products rose 50%.



Source: "The Future of U.S. Sugar Policy," McKeany-Flavell Company, Oakland, California, June 14, 2006

It is also likely that any potential savings on sugar would be too miniscule to even pass along to an individual shopper. That's because sweetener is just a fraction of the overall cost of a product, with a candy bar wrapper costing more than the sugar inside.

Dave DeCecco, a spokesman for Pepsi, was quoted in a July 2, 2006 *New York Times* article saying, "The cost of the sweetener in the product is extremely minimal to the point of not even mattering."

### **Are Sugar Prices Hurting Food Manufacturers Now?**

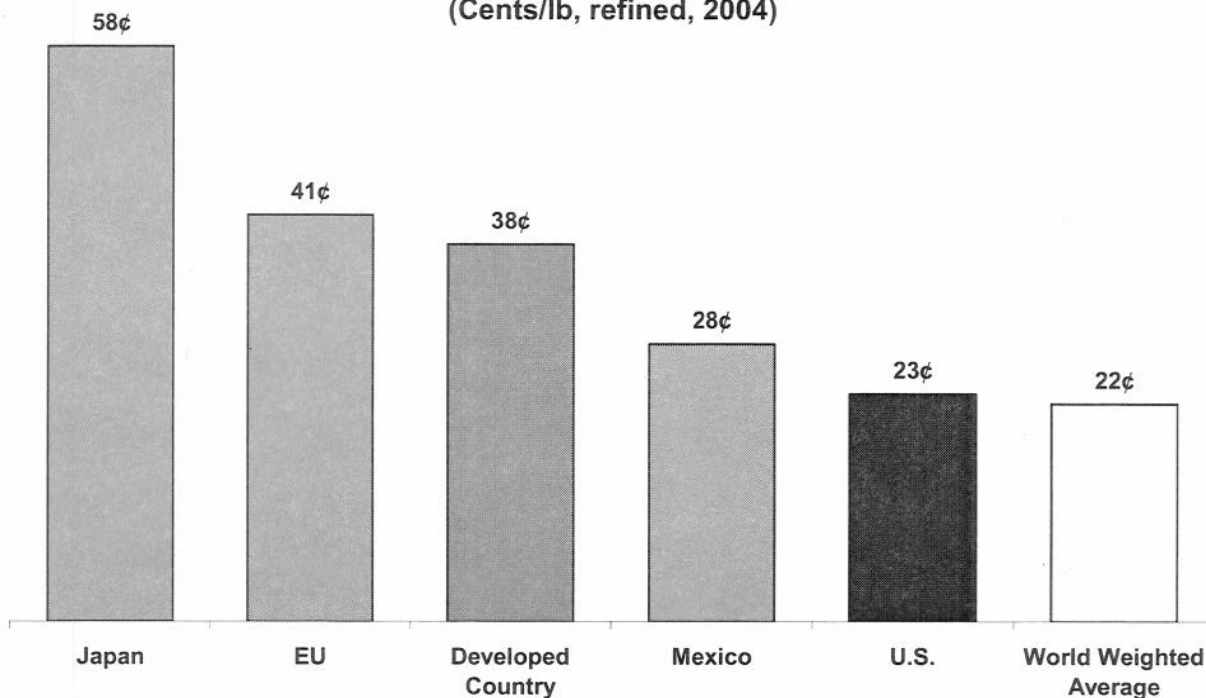
Like any business, food manufacturers' main objective is to make money, and driving down ingredient prices is just another way to do that. However, these companies aren't exactly getting gouged by sugar prices in the United States and their revenues aren't exactly slumping.

A 2005 study conducted by LMC International Ltd. about sugar prices around the globe showed that U.S. wholesale prices were on par with world prices in 2004.

In fact, the average U.S. wholesale price of 23 cents per pound was much lower than the EU price of 41 cents per pound or the developed-country average price of 38 cents per pound. Factor in developing nations, and the U.S. price was still comparable to a weighted world average of 22 cents a pound.

### Wholesale Refined Sugar Prices, North American and World

(Cents/lb, refined, 2004)



Source: LMC International Ltd, Oxford, England, June 2005: global survey of countries representing 77% of global sugar production.

When hurricanes Katrina, Rita, and Wilma wiped out huge swaths of sugarcane in Florida and Louisiana, there was a brief uptick in U.S. wholesale prices. This rise did not harm the food manufacturers though, because these companies purchased sugar contracts well before the hurricanes at much cheaper prices.

Page four of The Hershey Company's 2005 annual report summed up the situation.

*"The Company's costs for sugar will not necessarily reflect market price fluctuations primarily because of its forward purchasing and hedging practices...The Company believes that the supply of raw materials is adequate to meet its manufacturing requirements."*

Kraft Foods, another major sugar buyer, echoed this sentiment on page seven of its 2005 report to shareholders.

*"...the Company believes such raw materials to be in adequate supply and generally available from numerous sources. The Company uses hedging techniques to minimize the impact of price fluctuations in its principal raw materials."*

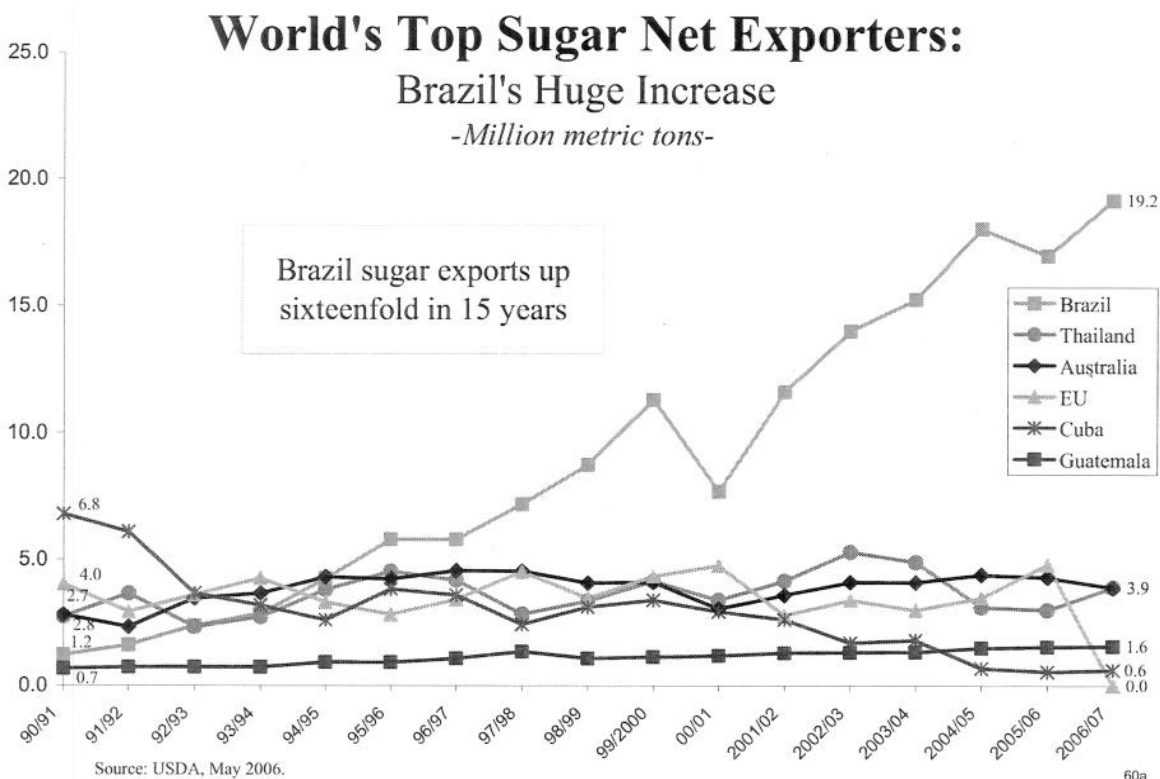
Truth be told, profits for industrial sugar users were stronger than ever, despite their claims of struggling to cope with sugar prices.

Nestlé Group, for example, posted record sales and profits in 2005. And in a February 7, 2006 press release, Bill Wrigley, Jr., Chairman, President & CEO of Wm. Wrigley Jr. Company, boasted: "The \$4-billion mark in sales is another significant milestone for the Company...our talented global team produced our ninth consecutive year of record earnings."

### How Would Brazil Win?

Three decades of ethanol subsidies propelled Brazil to the world's largest sugar exporter. According to USDA data, Brazil's sugar exports increased sixteenfold over the past 15 years, and today they export 19.2 million tons of sugar a year. And Brazil is still expanding its production.

By far the world's largest exporter, Brazil stands poised to gobble up any part of the U.S. market that is abandoned by U.S. companies bankrupted as a result of a sugar subsidy check system.



### How Would This Affect Other Foreign Suppliers?

Having one of the most open sugar markets on the planet, America is the world's second largest sugar importer, importing from 41 countries regardless of need. All but three of those countries are considered developing nations, and few of those developing nations could compete with the subsidies that Brazil doles out to its producers.

The American sugar market is particularly important for struggling countries because it is a stable market and because it offers prices that are fairer than poor producers would receive on the volatile world dump market, where foreign subsidies drive sugar prices below production costs. And the American market is even more important today after the European Union "reformed" its sugar policy to the detriment of many African nations.

Among the nations that would lose market share to Brazil if the current sugar program were scrapped: Argentina; Barbados; Belize; Bolivia; Colombia; Congo; Costa Rica; Cote D'Ivoire; Dominican Republic; Ecuador; El Salvador; Fiji; Gabon; Guatemala; Guyana; Haiti; Honduras; India; Jamaica; Madagascar; Malawi; Mauritius; Mozambique; Nicaragua; Panama; Papua New Guinea; Paraguay; Peru; Philippines; South Africa; St. Kitts and Nevis; Swaziland; Trinidad-Tobago; Uruguay; and Zimbabwe.

### Fast Facts: Brazil's Sugar Empire

- Brazil's sugar-ethanol program, built on decades of huge government subsidies, dominates the world sugar market.
- Since the early 1990s, Brazil has used the ethanol program to increase sugar exports from less than 2 million metric tons to nearly 20 million tons. Over that time, its share of the world sugar market jumped from 4% to more than 40%. Today, the country exports more sugar than the next six largest sugar exporters combined.
- The economic benefit to sugar producers from the ethanol program is estimated at \$1 billion a year.
- The Brazilian government provides more than \$200 million a year in direct subsidies to select sugar producers.
- Indirect subsidies—including \$2.1 billion in debt forgiveness, plus preferential loan rates and massive currency devaluations—have also aided Brazil's sugar expansion.
- Brazil, an agriculture superpower, still defines itself as a "developing" country in WTO negotiations to protect these subsidies and to avoid reform.
- The average Brazilian sugar worker earns 58 cents per hour and child labor remains an issue in the country.
- Even though the country has some environmental laws, it lacks an adequate monitoring program to track and curb pollution discharged by sugar mills and farms.
- By far the world's largest sugar player, Brazil produces 28 million tons of sugar. That's almost four times U.S. production.

## American Public Supports a Sugar Policy Extension

Given the clear division between winners and losers under a possible sugar subsidy check system, there's little wonder that the American public favors an extension of the existing program.

Nearly two-thirds (62%) of American adults believe that Congress should continue the current U.S. sugar policy, according to a May 2006 survey conducted by Harris Interactive.

Respondents were asked to choose between four sugar policy options for the upcoming Farm Bill debate: an extension of the current no-cost sugar program; an income support system similar to the policy of other farm commodities; a one-time buyout; and the elimination of the U.S. sugar program in favor of imports.

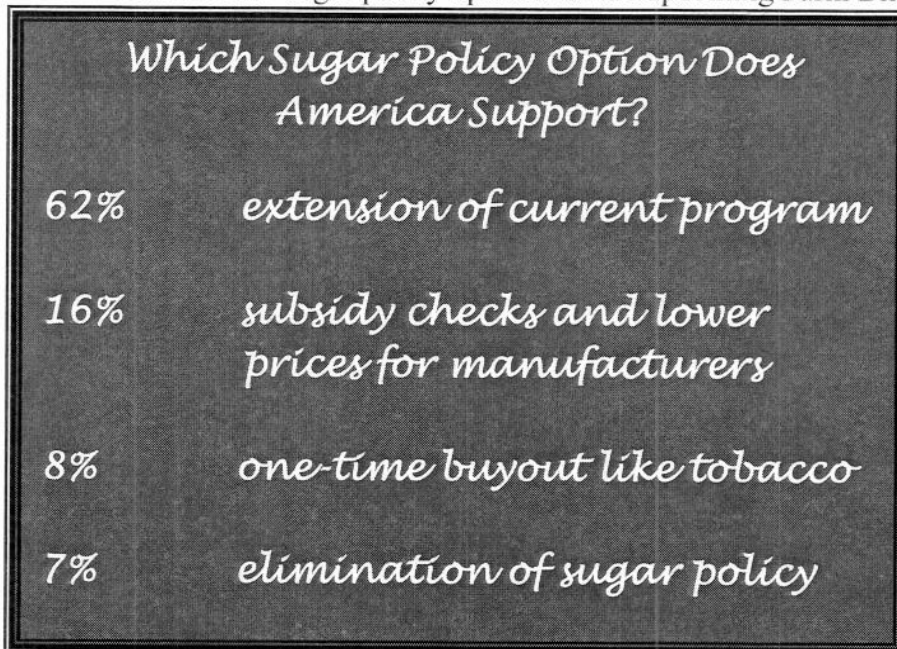
Only 16% of American adults supported transforming sugar to an income support program, even though they were told such a program would allow food

manufacturers to see cheaper sugar prices. A mere 8% thought a one-time buyout was a good idea, while only 7% supported the elimination of sugar policy.

Survey respondents were also asked a number of questions about sugar pricing and preferences between domestic or imported sugar. The results from those questions shed light on why the overwhelming majority thought an extension of the current program was a good idea.

Seven out of 10 Americans agree that sugar is inexpensive in the United States—an understandable response considering Americans spend more on 10 gallons of gasoline than they do on a year's worth of sugar.

The poll also showed that 93% of American adults feel it's somewhat or very important for our country to produce food at home instead of depending on foreign supplies. Even when told that foreign sugar might be cheaper, 72% of respondents said they'd prefer to buy American sugar. Only 7% said they favored foreign sugar.



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BACKING AMERICA'S BEET AND CANE FARMERS

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